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Dear Fellow East Siders:

In my discussions with many of our neighbors about the City's budget, I have repeatedly been asked whether Providence can restructure its finances (particularly its labor contracts) through the bankruptcy process. I spoke with some of the lawyers who are advising Providence and Central Falls about their finances. Here is what I found out:

There is a state process called receivership which was developed by the General Assembly last year in response to the crisis in Central Falls. The state receivership law does not authorize the receiver to restructure collective bargaining agreements (or the pension programs enshrined in those contracts).

There is a federal process that includes the authority to restructure collective bargaining agreements. It is called Chapter 9 federal bankruptcy. Federal law does not authorize cities to file for Chapter 9 bankruptcy unless they first obtain permission from the state. In Rhode Island, a city can get Chapter 9 permission in either of two ways. First, Providence may petition the General Assembly to pass a special law permitting such a filing. It is unlikely that the General Assembly will pass such legislation for Providence, as a bankruptcy in Providence would harm the State's credit rating, and possibly that of other communities. Alternatively, Providence could reach bankruptcy through the State receivership process, which authorizes the receiver to petition for bankruptcy if the State's process fails to resolve the city's financial problems. Now in its second year of state receivership, Central Falls may be headed towards this process.

Once the state receiver agrees to file for federal Chapter 9 bankruptcy, the court will not accept the filing unless it considers the city to be "insolvent" If a city has a reserve fund for its pension, it may have to spend down the reserve fund before it is "insolvent."

Even if a city is accepted for bankruptcy, the court cannot surgically remove labor contracts that contribute to the city's financial straits. Instead, the court will consider restructuring those contracts as part of a broader package that will likely include significant tax increases and reductions in city services. The New York Times reported in January on the federal bankruptcy of Vallejo, California that provides an instructive example you can review at this link: http://www.nytimes.com/2011/01/23/us/23bcweber.html?_r=1&scp=1&sq=vallejo&st=cse

Once a city successfully emerges from bankruptcy, businesses and people from other communities and states become reluctant to move there. In other words, a bankruptcy buys short term relief at a long term price of compromising future economic opportunities.

For these reasons, I do not believe the federal bankruptcy process (or the state receivership process) provides an easy solution that could relieve us from the difficult choices we currently face.

Sincerely,

