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Brazil court puts state firms ahead of bondholders in Rede case

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* Holdouts say state debt made whole at their expense

* Brazil seized Rede in August 2012 after cash crunch

By Guillermo Parra-Bernal

SAO PAULO, Sept 11 (Reuters) - Bondholders of Brazilian power holding company Grupo Rede Energia SA could lose as much as 75 percent of the value of their holdings after a court ruled that government-led creditors must be repaid in full, a sign of mounting risks for investors in Latin America's largest economy.

Rede Energia said on Monday that a bankruptcy court approved a takeover plan proposed by Energisa SA, which will pay 3 billion reais ($1.3 billion) for Rede's assets and assumed debt. As part of the deal, Energisa will pay Rede creditors about 1.9 billion reais and invest 1.1 billion reais in its eight distribution units to win regulatory approval.

Under terms of the plan, bondholders have up to 60 days to choose one of two repayment options, and the value of Rede's 11.125 percent perpetual bonds could be slashed by as much as three-fourths. According to calculations by Bank of AmericaMerrill Lynch analyst Alessandro Arlant, holdouts who fail to tender face a haircut of up to 90 percent.

"This is one more case of openly preferential treatment towards state-run creditors, an attitude that is detrimental to foreign investors and makes you wonder about the rule of law in Brazil," said a São Paulo-based holder of Rede Energia's perpetual debt, who declined to be identified because of the sensitivity of the issue. "This decision is clearly bondholder-unfriendly."

Government-run entities such as state development bank BNDES and Caixa Economica Federal's FI-FGTS workers' severance fund were fully repaid on a combined 960 million reais of claims with the decision, at the expense of bondholders. In a decision that investors see as unfriendly to their interests in Brazil, the court annulled bondholder trustee Bank of New York Mellon Corp's vote on the plan.

"There is no precedent in Brazil for this type of decision," a São Paulo-based banker said, referring to the court's decision to disregard BONY Mellon's vote. The banker, who declined to be identified because of the sensitivity of the issue, added that bondholders could appeal the ruling.

In a situation that some bondholders and the banker called "abnormal," the court allowed FI-FGTS to vote as a secured creditor, even though it was effectively a shareholder of Rede.

"In our view, it is possible this may introduce additional legal risk to other Brazilian corporates with complex ownership structures," analyst Arlant wrote.

An email sent to Caixa's press office seeking comment was not immediately answered, nor were calls to a BNDES spokesman in Rio de Janeiro.

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The Rede situation is not the first in which government creditors were given preferential treatment, BofA's Arlant noted. Last year, Equatorial Energia SA's acquisition of Rede's Celpa unit, in which a 234 million-real liability with BNDES was fully repaid at face value through shares, came with an 83 percent haircut for holdouts.

The price on the Rede Energia bond was about 23 cents on the dollar on Wednesday, barely unchanged from Tuesday.

Cash-strapped Rede Energia, which has more than 5 billion reais in outstanding debt, has been struggling since energy regulator Aneel seized eight of its units in August 2012 to prevent it from halting electricity service in six states. The units, power distributors in different parts of Brazil, were suffering from serious financial and operational problems.

Aneel's decision to seize Rede Energia came after the group's chairman and largest shareholder, Jorge Queiroz Jr., failed to sell part or all of his 54 percent stake. His stake was once valued at $600 million by some analysts.

Rede Energia declined to comment on the court's decision. Efforts to reach Queiroz, who is reportedly living outside of Brazil, were unsuccessful.

Dissatisfaction with the outcome of Rede Energia's debt restructuring process comes as defaults and unilateral moratoriums in Brazil may increase next year in the wake of weak economic growth, rising borrowing costs and a currency slump.

Eleazar de Carvalho, a senior partner at investment banking boutique **Virtus BR Partners**, said newfound caution among private-sector lenders could make it harder for some companies to refinance loans or bonds, or even obtain new financing.

Investors expect OGX Petróleo e Gas Participações SA , the struggling oil producer controlled by Brazilian tycoon Eike Batista, to launch a $3.6 billion bond restructuring - potentially the largest ever in Latin America - within days or weeks. OGX, which has repeatedly denied such a plan, recently hired Blackstone Group LP to help it "review its capital structure."

Currently OGX bonds due in 2018 and 2022, which trade at less than 20 cents on the dollar, are pricing a default. ($1 = 2.29 Brazilian reais) (Additional reporting by Anna Flávia Rochas; editing by Todd Benson and Matthew Lewis)

REDEENERGIA-BRAZIL/RESTRUCTURING | ABN | C | GRO | MTL | SOF | D | E | RBN | M | O | OIL | U

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