SOLVING INSOLVENT PUBLIC PENSIONS: THE LIMITATIONS OF THE CURRENT BANKRUPTCY OPTION

INTRODUCTION

Prichard, Alabama is a city of approximately 23,000[1] residents in the southwestern corner of the state. A dwindling population[2] and $3.9 million of debt forced Prichard to file for bankruptcy in 1999.[3] After emerging from bankruptcy in 2007,[4] the city filed again in October of 2009, this time in the shadow of a lawsuit by pensioners questioning the solvency of their city pensions.[5] Prichard stopped paying pensions and the bankruptcy judge denied the pensioners' claim to their pensions during the proceedings.[6] The judge dismissed the case in March of the following year; however, Prichard failed to resume payments.[7] Nearly two years after pension payments stopped, Prichard announced a settlement with its retirees that would give them only one third of their promised pay.[8] Prichard is currently awaiting a ruling from the Alabama Supreme Court to determine whether their bankruptcy case can proceed.[9]

The case of Prichard, Alabama is certainly unique in its circumstances, history, and financial and political challenges. It highlights, however, what is

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1 *State and County Quickfacts*, U.S. CENSUS BUREAU, http://quickfacts.census.gov/qfd/states/01/0162496.html (last visited Nov. 11, 2011).

2 Michael Cooper & Mary Williams Walsh, *Alabama Town's Failed Pension is a Warning*, N.Y. TIMES, Dec. 22, 2010, http://www.nytimes.com/2010/12/23/business/23prichard.html (noting that Prichard, Alabama has shrunk by nearly forty percent since the 1970s).

3 Douglas J. Watson, Donna Handley & Wendy L. Hassett, *Financial Distress and Municipal Bankruptcy: The Case of Prichard, Alabama*, 17 J. PUB. BUDGETING ACCT. & FIN. MGMT. 129, 142 (2005).

4 David Ferrara, *Prichard Files for Bankruptcy Protection; City Faces Lawsuit Over Nearly Empty Pension Fund*, AL.COM (Oct. 28, 2009, 7:02 AM), http://blog.al.com/live/2009/10/prichard_files_for_bankruptcy_1.html.

5 David Ferrara, *After Bankruptcy Case Gets Tossed, Prichard Retirees Sue City*, AL.COM (Sept. 2, 2010, 6:00 AM), http://blog.al.com/live/2010/09/after_bankruptcy_case_gets_tos.html.

6 Order Denying Prichard Retirees' Motion for Administrative Claim and to Compel Payment of Administrative Expenses, *In re* City of Prichard, No. 09-15000-WSS (Bankr. S.D. Ala. Mar. 10, 2010); David Ferrera, *Motion to Force Prichard to Pay Pensioners Denied by Judge*, AL.COM (March 10, 2010, 6:34 AM), http://blog.al.com/live/2010/03/motion_to_force_prichard_to_pa.html.

7 Ferrara, *supra* note 5.

8 Katherine Sayre, *Prichard Pension Crisis: Judge Approves Settlement; Payments to Restart Next Month*, AL.COM (May 25, 2011, 5:46 PM), http://blog.al.com/live/2011/05/judge_approves_prichard_pensio.html.

9 *In re* City of Prichard, No. 1:10-00622-KD-M, 2011 U.S. Dist. LEXIS 68747, at *4 (S.D. Ala. May 17, 2011).

likely to be an increasingly frequent problem for municipalities across the United States.[10] The problems of municipalities that are unable to pay their pension obligations are similar to the basic problem of any debtor in bankruptcy: the debtor (in this case the municipality) has taken on more debt (including pension obligations, among other debt) than it can afford to pay. However, these problems are also uniquely political and have a very direct public impact.[11] Municipalities are faced with the conundrum of how to provide adequate protection for pensioners without either (a) crippling municipal services and the basic operations of their governmental unit or (b) disproportionately pushing pension obligations onto the current and future municipal workforce and future taxpayers.

The state law tools available for municipalities to manage these pension obligations are limited.[12] Chapter 9, the portion of the Bankruptcy Code governing municipal bankruptcy, offers what may be a last resort for many municipalities unable to pay pension obligations. "Chapter 9 is intended to enable a financially distressed municipality to 'continue to provide its residents with essential services such as police protection, fire protection, sewage and garbage removal, and schools[],' while it works out a plan to adjust its debts and obligations."[13] Importantly, federal law requires that states authorize municipal bankruptcy,[14] which a majority of states have failed to do.[15] As such, municipalities in a majority of states are left without access to chapter 9.[16] Chapter 9 does not explicitly contemplate pensioners as debtors,[17] and

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10 Bill Vidonic & Debra Erdley, *Pension Crisis Extends Far Beyond Pittsburgh*, PITTSBURGH TRIB.-REV., Nov. 8, 2010, http://www.pittsburghlive.com/x/pittsburghtrib/news/s_708214.html; *Pension Review Panel Meets to Discuss Options for Atlanta's Pension Plan*, CITY OF ATLANTA, http://www.atlantaga.gov/media/nr_pension_022210.aspx (last visited Jan. 4, 2011); *see also* Liam Dillon, *Explainer: Are Pensions Fair Game in Bankruptcy*, VOICEOFSANDIEGO.ORG (Feb. 15, 2010, 6:11 PM), http://www.voiceofsandiego.org/government/article_0418be36-1aa3-11df-840f-001cc4c03286.html (showing that ongoing public suggestions indicate that municipal bankruptcy might be an appropriate remedy for the reported $2.1 billion in pension obligations that the city owes).

11 *See, e.g.*, Charles Duhigg, *Public Unions Take on Boss to Win Big Pensions*, N.Y. TIMES, June 21, 2011, http://www.nytimes.com/2011/06/22/business/22union.html (discussing the fact that Costa Mesa, CA had a $100,000 public-union-funded opposition campaign to a pension reform candidate).

12 *See, e.g.*, Navlet v. Port of Seattle, 194 P.3d 221, 232 (Wash. 2008) (en banc).

13 *In re* City of Bridgeport, 129 B.R. 332, 336–37 (Bankr. D. Conn. 1991) (quoting H.R. REP. NO. 100-1011, at 2 (1988), *reprinted in* 1988 U.S.C.C.A.N. 4115, 4116) (citation omitted).

14 11 U.S.C. § 109(c)(2) (2006).

15 Only nineteen states currently authorize municipal bankruptcy. *Issue Summary: Municipal Bankruptcy*, ALLEGHENY INSTITUTE, http://www.alleghenyinstitute.org/government/munbankruptcy.html (last visited Jan. 5, 2011).

16 *Id.*

17 *See* 11 U.S.C. § 901. *But see* 11 U.S.C. §§ 1113–1114.

Congress has recognized the need to study pension issues in municipal bankruptcy.[18] However, to date, Congress has not modified chapter 9 to address potential pension concerns.[19]

Changes in local practice, state laws, and federal laws are necessary to give municipal governments tools to manage pension debt. Local governments can, and should, take preventative measures to ensure that retirement obligations do not limit their future ability to provide basic government services while simultaneously honoring obligations to pensioners. However, these preventative measures alone will not provide the relief needed for many municipalities in crisis. Neither state legal structures nor federal municipal bankruptcy law, as they presently exist, can provide the more immediate relief that municipalities need, especially given the unique voter-employee, government-employer dynamics. For municipalities to continue providing essential governmental services, provisions should be added to state law to ensure that chapter 9, when used to manage pension debt, is both politically feasible and fair to pensioners. Additionally, provisions should be added to chapter 9 guaranteeing greater municipal employee protections for these same purposes.

This Comment first summarizes current economic factors driving the recent increased likelihood of municipal insolvency, explores the unique taxpayer and voter constituency impacting municipal bankruptcy, and provides a brief background of municipal bankruptcy law. This Comment then reviews the legal framework surrounding municipalities' options for managing pension obligations, including state pension and labor law. Subsequently, this Comment contrasts the process by which a pension is discharged and the manner in which employee pensions are protected in traditional chapter 11 bankruptcy as compared to chapter 9. Next, this Comment suggests how chapter 9 might enable a municipality to reduce or discharge pension obligations and highlights the gaps in such a process. Finally, this Comment proposes changes in local practice and state and federal law that are necessary to allow municipalities in crisis to fairly and effectively manage pension obligations.

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[18] *See* H.R. REP. NO. 102-459, at 368 (1992) ("The depressed economic situation . . . has raised a number of important questions, including the treatment of labor agreements, pensions, health benefits, et cetera. The subcommittee may wish to review the impact of municipal bankruptcy in these areas.").

[19] Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, 119 Stat. 23.

I. BACKGROUND

A. *Current Economic Conditions and Stakeholders*

1. *Federal, State, and Municipal Revenue and Debt Crises*

Municipal bankruptcy has been a rarity since Congress first authorized it in 1934.[20] However, reduced municipal revenues, coupled with increased municipal obligations, have given rise to speculation that more municipalities will consider this tool in the future.[21] Moreover, Standard & Poor's recent historic downgrade of the United States' credit rating has led some to speculate that this national debt uncertainty could lead to further instability in the municipal bond market.[22]

Municipal bond defaults are rare.[23] Moody's reports only fifty-four defaults of their rated municipal bonds since 1970, and of these, only three were defaults of general obligation debt.[24] However, the municipal bond default trend suggests that they are becoming more common, with 13% of the defaults in the last forty years occurring in the 2008-2009 period.[25] During that time frame, an increased number of municipal bond ratings were downgraded.[26]

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[20] *See* Nicholas McGrath & Ji Hun Kim, *The Next Chapter for Municipal Bankruptcy*, AM. BANKR. INST. J., June 2010, at 14, 14 ("[T]here have only been approximately 566 [c]hapter 9 filings.").

[21] *See, e.g.*, *id.* at 14; Robert J. Landry III & Keren H. Deal, *More Municipalities Likely to Face Chapter 9: Is a Perfect Storm Brewing?*, AM. BANKR. INST. J., July–Aug. 2008, at 18, 72; Ianthe Jeanne Dugan & Kris Maher, *Muni Threat: Cities Weigh Chapter 9*, WALL ST. J., Feb. 18, 2010, http://online.wsj.com/article/SB10001424052748704398804575071591602878062.html. *But see* Ameet Sachdev, *Municipal Bankruptcy Fears Overblown, Official Says*, CHI. TRIB., Sept. 21, 2010, http://articles.chicagotribune.com/2010-09-21/business/ct-biz-0921-chicago-law-20100921_1_bankruptcy-cases-municipal-bankruptcy-debts (arguing there will be an increase in municipal bond restructuring, but that such actions will be short of filing for municipal bankruptcy).

[22] *See* Kathy Bergen, Kristen Mack & Monique Garcia, *Debt-rating Deluge Could Trickle Down to Cities and States*, CHI. TRIB., Aug. 9, 2011, http://articles.chicagotribune.com/2011-08-09/business/ct-biz-0809-downgrade-bonds-20110809_1_rating-downgrade-mcdonnell-investment-management-llc-credit-ratings.

[23] *See infra* notes 244–47 and accompanying text.

[24] MOODY'S INVESTORS SERVICE, U.S. MUNICIPAL BOND DEFAULTS AND RECOVERIES, 1970–2009, at 2 (2010), *available at* http://v2.moodys.com/cust/content/Content.ashx?source=StaticContent/Free%20Pages/Regulatory%20Affairs/Documents/us_municipal_bond_defaults_and_recoveries_02_10.pdf (finding that a majority of these defaults were in areas of specific government focus, namely the healthcare and housing project finance sector).

[25] *Id.* at 2, 12–13 (finding seven defaults in the 2008–2009 period and fifty-four between 1970–2009); *see also infra* notes 244–47 and accompanying text.

[26] U.S. MUNICIPAL BOND DEFAULTS AND RECOVERIES, *supra* note 24, at 7.

A substantial portion of municipal revenue is dependent upon property values,[27] so when these values decline, cities are hit hard.[28] The exact percentage of municipal funding from property tax varies, but averages 71.4% of local tax revenue.[29] The third quarter of 2010 marked the seventeenth consecutive quarter of falling home values,[30] and foreclosures hit record highs in 2010.[31] In Clark County, Nevada, which includes Las Vegas, 71.1% of homeowners owed more on their homes than they were worth as of September 31, 2010.[32]

During this tight budget period, federal funding was appropriated in the American Recovery and Reinvestment Act (ARRA),[33] in part to fill the gaps for state and local governments.[34] Congress enacted ARRA in February 2009 for the purpose of stimulating the United States economy and "[stabilizing] State and local government budgets, in order to minimize and avoid reductions in essential services and counterproductive state and local tax increases."[35] Funding from ARRA accounted for $60 billion of the states' $192 billion shortfall in fiscal year 2010.[36] Additionally, this federal stimulus package provided discretionary spending for local governments in the form of grants to local law enforcement, firefighters, and other funds.[37]

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27 MELISSA BRAYBROOKS, JULIO RUIZ & ELIZABETH ACCETTA, STATE GOVERNMENT TAX COLLECTIONS SUMMARY REPORT: 2010, at 5 (2011), *available at* http://www2.census.gov/govs/statetax/2010stcreport.pdf (indicating in a 2007 Census of State Governments report that the average municipality received 71.4% of revenue from property taxes).

28 Sioban Hughes, *For Strapped Cities, a New Normal*, WALL ST. J., Sept. 27, 2011, http://online.wsj.com/article/SB10001424052970204831304576596973923470178.html (discussing a National League of Cities survey that found that revenue declines, largely from property tax declines, had led to fee increases, layoffs, and salary freezes in many cities).

29 BRAYBROOKS, RUIZ & ACCETTA, *supra* note 27, at 5.

30 Steve Goldstein, *Home Values Down for 17th Straight Quarter: Report*, WALL ST. J., Nov. 10, 2010, http://www.marketwatch.com/story/home-values-down-for-17th-straight-quarter-report-2010-11-10.

31 William Alden, *Foreclosures Hit Record High in August*, HUFFINGTON POST, Sept. 16, 2010, http://www.huffingtonpost.com/2010/09/16/foreclosures-hit-record_n_719912.html.

32 *Chart: Owing More Than Home Is Worth*, USA TODAY, Feb. 8, 2011, http://www.usatoday.com/money/economy/housing/2011-02-04-under-water-chart_N.htm.

33 American Recovery and Reinvestment Act of 2009, Pub. L. No. 111-5, 123 Stat. 115 [hereinafter Federal Stimulus Package].

34 Shawn Tully, *Meredith Whitney's New Target: The States*, FORTUNE, Sept. 28, 2010, http://finance.fortune.cnn.com/2010/09/28/meredith-whitneys-new-target-the-states/.

35 Federal Stimulus Package, *supra* note 33, § 3(a)(5).

36 Tully, *supra* note 34.

37 Federal Stimulus Package, *supra* note 33, §§ 105, 509 (including funding for local law enforcement, local disaster assistance, firefighter, and school funding, among other funds directed to local governments).

There was no comparable federal funding in federal fiscal year 2011,[38] however, and many states are implementing draconian budget cuts[39] or tax increases[40] to try to make up for current shortfalls. Additionally, Congress's August 2011 debt-ceiling deal called for $900 million in federal budget cuts over the next decade, which will invariably impact out-year federal aid to states.[41] With state funding providing roughly one third of municipal budgets, it is reasonable to assume that these local governments will experience increased challenges in their ability to remain current on municipal debt obligations and in their ability to provide essential public services to citizens.[42] These revenue pressures have left municipalities particularly vulnerable to the consequences of declining revenue sources and poor investment strategies.[43]

2. *Municipal Legal Obligations*

In the face of decreasing revenues and eroding tax digests, municipalities are often faced with increasing "legacy obligations."[44] These legacy

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38 The "Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010" signed by President Obama on December 17, 2010 includes a 2% cut to 2011 Social Security taxes among other tax cuts including extension of the group of income tax and other tax cuts that have been referred to as the "Bush tax cuts." Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010, Pub. L. No. 111-312, 124 Stat. 3296. This tax cut package has been considered by some to be another federal stimulus bill. *See, e.g.*, *U.S. Tax Bill Is Stimulus in Disguise*, Interview by Jason Stipp with Bob Johnson, Director of Economic Analysis, Morningstar (Dec. 13, 2010), *available at* http://www.morningstar.co.uk/uk/news/article.aspx. However, even if the Act is viewed as a stimulus, it is not in the form of funds made directly to state or local governments.

39 Andrew Heining, *Schwarzenegger Calls for Deep California Budget Cuts*, CHRISTIAN SCI. MONITOR, May 15, 2010, http://www.csmonitor.com/USA/Politics/2010/0515/Schwarzenegger-calls-for-deep-California-budget-cuts.

40 Randal C. Archibold, *In Arizona's Latest Twist, Voters Follow G.O.P. Governor and Approve Tax Increase*, N.Y. TIMES, May 19, 2010, http://www.nytimes.com/2010/05/20/us/20tax.html.

41 *See* Michael A. Fletcher, *With Debt Deal, States Brace for Cuts in Federal Aid*, WASH. POST, Aug. 2, 2011, http://www.washingtonpost.com/business/economy/with-debt-deal-states-brace-for-cuts-in-federalaid/2011/08/02/gIQANdRWqI_story.html.

42 Tully, *supra* note 34 (predicting that the widening gap between local government spending and revenues puts municipal bonds at risk). *But see* Nelson D. Schwartz, *A Seer on Banks Raises a Furor on Bonds*, N.Y. TIMES, Feb. 7, 2011, http://www.nytimes.com/2011/02/08/business/economy/08whitney.html (discussing critics' belief that speculation that the municipal bond market is in trouble is overstated).

43 Lisa Lambert, *Special Report: The Incinerator That May Burn Muni-Investors*, REUTERS, May 12, 2010, http://www.reuters.com/article/idUSTRE64B2PM20100512 (noting that Harrisburg's interest on the debt for a trash burning plant left the city with $3 million more in interest payments on the debt in 2010 than the city's budget).

44 *See Kaiser Aluminum Files for Chapter 11 Protection; Cites Asbestos Suits*, ANDREWS DEL. CORP. LITIG. REP., Mar. 2002, at 1, 10 ("Kaiser Aluminum Corp. filed for chapter 11 bankruptcy protection citing 'unwieldy legacy obligations including asbestos litigation.'"); George McGregor, *The Implications of GASB 45 on Early Retirees*, J. COMPENSATION & BENEFITS, Nov.–Dec. 2009, at 17, 18 (defining benefit pension

obligations often include payments to retirees.[45] For example, municipalities may be obligated to provide for pensions[46] or "other post employment benefits"[47] such as retiree healthcare.[48] While these "other post-employment benefit" liabilities are certainly pressing issues for many state and local governments,[49] there are often unique and, at times more flexible, state laws that govern these benefits.[50] As such, discussing these benefits in municipal bankruptcy is beyond the scope of this Comment. Rather, this Comment will focus on municipal pension obligations, a form of legacy obligation with often strict state statutory and constitutional limitations that prevent the municipality from reducing benefits to prevent insolvency.[51]

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plans, Social Security, and Medicare and Medicaid are given as examples of "legacy obligations"); Mark J. Roe & David Skeel, *Assessing the Chrysler Bankruptcy*, 108 MICH. L. REV. 727, 759 n.78 (providing the example of legacy costs as being "'health-care and other benefits for the company's 85,000 retirees'" (quoting Robert Guy Matthews, *W.L. RossFirm to Buy LTV Assets for $125 Million*, WALL ST. J., Feb. 28, 2002, at A6)).

45 *See, e.g.*, Hal Dardick, *Chicago Faces Crisis Over Pension Funding, How to Pay for It*, CHI. BREAKING NEWS CTR., Oct. 18, 2010, http://www.chicagobreakingnews.com/2010/10/chicago-faces-crisis-over-pension-funding-how-to-pay-for-it.html.

46 *See, e.g.*, *id.*

47 Jenna Amato Moran, *The OPEB Tsunami: Riding the Wave of Public Sector Postemployment Health Benefits*, 58 BUFF. L. REV. 677, 677, 682 (2010) (discussing the Governmental Accounting Standards Board (GASB)'s promulgation of new standards for the reporting of "other postemployment benefit" or OPEB liability, which consists of non-pension post-employment benefits including retiree healthcare expenses).

48 *See, e.g.*, Martin Z. Braun, *New York City's Retiree Health Costs Increase 14.5 Percent to $75 Billion*, BLOOMBERG, Dec. 10, 2010, http://www.bloomberg.com/news/2010-12-10/new-york-city-s-retiree-health-costs-rise-14-5-to-75-billion-on-reform.html; Catherine Kavanaugh, *Retiree Healthcare Strains City Budget*, DAILY TRIB. (Oakland Cnty., Mich.), Jan. 8, 2011, http://www.dailytribune.com/articles/2011/01/08/news/doc4d29042cc1bc7926684857.txt.

49 The new GASB accounting standards shifted from what was a "pay-as-you-go" model to one that requires government employers to "calculate the present amount it expects to pay out for OPEB for its current retirees and employees. The employer must then take this number and determine what annual contribution is required in order to adequately fund its OPEB liability over thirty years." Moran, *supra* note 47, at 684–85. These new standards essentially created "new" massive unfunded liabilities for state and local governments. *See, e.g.*, Braun, *supra* note 48 (reporting that New York City was saddled with $75 billion in retiree and other post employment benefit liability which outstripped the $42.2 billion in reported pension unfunded liability).

50 *See, e.g.*, Doyle v. City of Medford, 606 F.3d 667, 669 (9th Cir. 2010) (holding that retiree health insurance benefits were not a property right protected by the Due Process clause of the U.S. Constitution); Lippman v. Bd. of Educ., 487 N.E.2d 897, 898 (N.Y. 1985) (finding the local board of education's decision to reduce their share of retiree healthcare premiums did not violate the state constitutional mandate protecting pensions as contractual relationships, as "there was no contract, express or implied, by respondent Board of Education not to reduce its contribution to payment of health insurance premiums of retired employees and their dependents"). *But see* Am. Fed'n of State, Cnty. and Mun. Emp. v. City of Benton, 513 F.3d 874, 882 (8th Cir. 2008) (finding the City's elimination of certain retiree healthcare benefits was a violation of the retirees' constitutional rights to contract because the benefits were specified in the collective bargaining agreement).

51 *See, e.g.*, Navlet v. Port of Seattle, 194 P.3d 221, 232 (Wash. 2008) (en banc) ("It is the law of this State that an employee has a vested right in the pension *or retirement system* in effect when he becomes a

In light of the many revenue and budgetary pressures faced by municipalities, including declining property tax, employment tax, and sales tax income, additional difficulties result when local governments attempt to make up the shortfalls in pension revenues by drawing down pension reserves or funds from pension trusts and from funding pension obligations by continuing current employee contributions. When faced with declining public employment and shrinking pension trust reserves, the strategic decision to fund pension obligations by these dwindling revenue sources is not economically viable.

3. Municipal Obligation, Political Pressures, and Legal Limitations

The multiple and intertwined constituencies involved in municipal pension obligations cause any potential solution to be subject to political pressures that may not be present to the same degree in chapter 11.[52] Municipal employees entitled to a pension, both those presently working and those retired, are in many cases also taxpayers footing the bill for municipal obligations, and more importantly, voters choosing whether to keep "management" in office.[53]

The individual residents and businesses that are paying taxes, purchasing goods and property, and employing residents within a municipality have the ability to relocate. This competitive pressure drives what has been described as a "tax maximization" point[54] where, at some level, municipal taxes are so high, the expected revenue cannot be raised.[55] Additionally, individual municipal residents are also voters, and thus any municipal government action is subject to resident oversight that is not in any way diminished during bankruptcy or other state debt management actions. This can be contrasted with the role of

qualified employee, or which becomes effective during his employment, and that system cannot be altered to his detriment without a corresponding benefit to him." (quoting Abels v. Snohomish Cnty. Pub. Util. Dist. No. 1, 849 P.2d 1258, 1265 (Wash. Ct. App. 1993))).

52 5 WILLIAM L. NORTON, JR. & WILLIAM L. NORTON III, NORTON BANKRUPTCY LAW AND PRACTICE 3D § 91:1 (2008) (explaining that chapter 11 is the portion of the Bankruptcy Code that governs bankruptcy proceedings initiated by the debtor where, in most cases, the debtor remains as the debtor-in-possession).

53 In many states, there is also a municipal worker labor union or unions that are charged with representing the interests of current employees which creates an additional dynamic in employer/employee relations. *See, e.g.*, AFSCME, http://www.afscme.org/home (last visited Oct. 12, 2011).

54 Michael W. McConnell & Randal C. Picker, *When Cities Go Broke: A Conceptual Introduction to Municipal Bankruptcy*, 60 U. CHI. L. REV. 425, 466 (1993).

55 *Id.* at 466 n.186 (citing *In re* Sanitary and Improvement Dist., #7, 98 B.R. 970, 976 (Bankr. D. Neb. 1989)); *see also* Wright v. City of Coral Gables, 137 F.2d 192, 196 (5th Cir. 1943) (Waller, J., concurring in part and dissenting in part) ("[I]f special further Court-ordered and enforced levies were made the rate of taxation would be so high as to prevent property owners from paying their taxes . . . ."), *aff'd*, 321 U.S. 753 (1944).

shareholders in a chapter 11 reorganization. While shareholders often have a similar voter-constituency sway over management of a public company, their financial interests are no longer primary.[56] Thus, in a chapter 11 bankruptcy proceeding, the court requires that management make decisions in the best interest of the debtor's estate, rather than in the interest of shareholders.[57]

Other than pensioners, a municipality's creditors are, by and large, "faceless" municipal bondholders that in most cases reside far away from the municipality. Coupled with the dynamics of the voter and taxpayer constituency, this can contribute to a decision-making bias that might encourage elected officials to place the interests of current residents and taxpayers before the interests of creditors.

Finally, because the municipality receives its authority through the state in which it resides,[58] the municipality is governed by state laws regarding debt and pension obligations[59] and potentially subject to, and sometimes the beneficiary of, state intervention in the case of a distressed or insolvent municipality.[60] The needs and interests of all of these parties contribute to an environment that is far more politicized than bankruptcies in chapter 11. These political pressures must be considered when drafting or amending chapter 9.

B. Tools Available Under Chapter 9

Chapter 9 of title 11 of the U.S. Code (the "Code") provides a federal system for restructuring municipal debts.[61] Importantly, chapter 9 of the Code

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[56] Martin J. Bienenstock, *Once in Bankruptcy, Whose Company is it Anyways?*, *in* CURRENT DEVELOPMENTS IN BANKRUPTCY AND REORGANIZATION 1991, at 667, 679 (PLI Comm. Law & Practice, Course Handbook Ser. No. A4-4333, 1991) ("One of the most painful facts of bankruptcy is that the interests of shareholders become subordinated to the interests of creditors." (internal quotation marks omitted)).

[57] *See, e.g.*, C.W. Mining Co. v. Aquila, Inc. (*In re* CW Mining Co.), 636 F.3d 1257, 1265 (10th Cir. 2011), *cert. denied*, No. 10-1412, 2011 WL 4530206 (Oct. 3, 2011) (stating that the purpose of the debtor's continued existence is to "maximiz[e] the value of the estate for its creditors, not its shareholders").

[58] *See, e.g.*, FLA. CONST. art. VIII, § 2 (specifying the process by which state law can establish municipalities); Jonathan J. Spitz, *Federalism, States and the Power to Regulate Municipal Bankruptcies: Who May Be a Debtor Under Section 109(c)*, 9 BANKR. DEV. J. 621, 630 (1993) ("A municipality is merely a department of the State, and *the State may withhold, grant or withdraw powers as it sees fit*.").

[59] *See, e.g.*, 53 PA. STAT. ANN. § 895.101-.803 (West 2011); FLA. STAT. ANN. § 185.01-.60 (West 2011).

[60] *See, e.g.*, Heather M. Forrest, *State Court Receivership Alternative to Chapter 9*, AM. BANKR. INST. J., Oct. 2010, at 12, 83 (discussing a Rhode Island state law that requires a fiscal overseer and other requirements in the case of a municipal fiscal emergency).

[61] 11 U.S.C. § 109(c)(2) (2006) (providing that a municipality's access to chapter 9 is conditioned upon the state's authorization).

excludes several provisions that would otherwise apply in chapter 11[62] and includes unique protections for the municipal debtor prompted, in part, by federalism concerns.[63] To put the options available to municipalities under today's bankruptcy laws in context, it is helpful to understand the history of municipal bankruptcy statutes.

1. *A Brief History of Municipal Bankruptcy*

The predecessors to today's federal municipal bankruptcy statutes were first enacted in 1934 in the wake of the Great Depression.[64] During the Great Depression, there were reportedly 2,019 municipalities in default in the United States.[65] Congress originally authorized municipal access to the Code because states were constitutionally limited from impairing contracts and thus the states were "powerless to assist municipalities."[66] The Supreme Court declared this first municipal bankruptcy act unconstitutional in *Ashton v. Cameron County Water Improvement District* in 1936 because the act was held to impair state sovereignty.[67] Congress responded by passing an amended municipal bankruptcy act[68] containing a number of new requirements for entering municipal bankruptcy and other state protections. This act was upheld by the Supreme Court in *United States v. Bekins.*[69]

The federal municipal bankruptcy statutes were overhauled in 1976 partially in response to New York City's fiscal crisis.[70] While these changes were implemented to enable big cities to more readily invoke the protections of municipal bankruptcy, they served to make bankruptcy more accessible to municipalities in general.[71] The 1976 revisions removed the requirement that a

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62 *See, e.g.*, 11 U.S.C. § 109; *Id.* §§ 1113–1114.

63 Spitz, *supra* note 58, at 626.

64 Municipal Bankruptcy Act of 1934, Pub. L. No. 251, 48 Stat. 798 (1934) *invalidated by* Ashton v. Cameron Cnty. Water Improvement Dist. No. 1, 298 U.S. 513 (1936).

65 Spitz, *supra* note 58, at 622.

66 *Id.*

67 *Ashton*, 298 U.S. at 531 ("The sovereignty of the state essential to its proper functioning under the Federal Constitution cannot be surrendered; it cannot be taken away by any form of legislation.").

68 McConnell & Picker, *supra* note 54, at 427–28.

69 United States v. Bekins, 304 U.S. 27, 50–51 (1938) ("The statute is carefully drawn so as to not impinge upon the sovereignty of the State.").

70 ADVANCED CHAPTER ELEVEN BANKRUPTCY PRACTICE § 15.5, at 436 (Thomas. J. Salerno et. al. eds. 1996 & Supp. 2010) ("Municipal bankruptcy law remained largely unchanged until 1976. Then the financial crisis of New York City appeared to be leading to a municipal bankruptcy. That created a great deal of reanalysis of municipal reorganizations and a review of bankruptcy law's usefulness for major municipal entities.").

71 5 NORTON, *supra* note 52, § 90:2.

municipality obtain the prepetition consent of greater than 50% of its creditors and enabled a municipality to continue borrowing to provide essential services to citizens throughout the duration of the bankruptcy.[72]

2. *Chapter 9 Petitioner Requirements*

Given that municipalities are public entities protected by the Tenth Amendment to the U.S. Constitution,[73] chapter 9 is unique from its consumer and business counterparts.[74] Notably, all municipal bankruptcy filings must be voluntary and cannot be initiated by a creditor.[75] Additionally, there is no process under federal municipal bankruptcy law for liquidation of the municipality.[76]

There are five requirements to qualify as a debtor under chapter 9:[77] (1) The petitioner must be a municipality, which is defined as a "political subdivision or public agency or instrumentality of a state";[78] (2) the petitioner must be insolvent; (3) the petitioner must desire a plan to adjust its debts;[79] (4) the petitioner must be authorized by the state to access chapter 9;[80] and (5) the petitioner must engage in good faith negotiations prior to filing the petition unless such negotiations are impractical or a municipality "reasonably believes that a creditor may attempt to obtain a preference."[81]

The fourth requirement, that the state specifically authorize municipal access to the Code, limits most municipalities from employing this tool. Currently, nineteen states authorize municipal bankruptcy in some form.[82]

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72 1 NORTON, *supra* note 52, § 3-A:4.

73 U.S. CONST. amend. X ("The powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States respectively, or to the people."); *see also In re* Sullivan Cnty. Reg'l Refuse Disposal Dist., 165 B.R. 60, 73 n.41 (Bankr. D.N.H. 1994) ("A municipality has only those powers granted by the state. Unless state law has authorized the municipality to seek protection under federal law, use of the Bankruptcy Code would implicate the Tenth Amendment to the U.S. Constitution.").

74 5 NORTON, *supra* note 52, § 90:4.

75 *See* 11 U.S.C. §§ 301, 303(a), 901(a) (2006).

76 *See id.* § 901(a).

77 *Id.* § 109(c); 5 NORTON, *supra* note 52, § 90:5.

78 11 U.S.C. § 101(40).

79 This requirement is meant to deter municipalities from filing solely to evade creditors. Nicholas B. Malito, *Municipal Bankruptcy: An Overview of Chapter 9 and a Critique of the "Specifically Authorized" and "Insolvent" Eligibility Requirements of 11 U.S.C.A. § 109(c)*, 17 NORTON J. BANKR L. & PRAC. 517, 525 (2008).

80 11 U.S.C. § 109(c)(2).

81 5 NORTON, *supra* note 52, § 90:5.

82 ALLEGHENY INSTITUTE, *supra* note 15.

Within these states, there is a range of approaches to authorization, including blanket authorization of chapter 9[83] and discretionary systems that condition access to chapter 9 upon consent of the Governor or a municipal finance commission.[84] One state explicitly forbids all municipalities within the state from filing for bankruptcy.[85] The majority of states have not expressly addressed this point by statute.[86] While the authorization requirement has existed since the enactment of the Code, the 1994 amendments[87] changed the authorization requirement from "general" to "specific" authorization.[88] Specific authorization "must be 'exact, plain, and direct with well-defined limits so that nothing is left to inference or implication.'"[89] Accordingly, most states do not authorize chapter 9 bankruptcy relief. The lack of state authorization has left some financially distressed municipalities clamoring for their state to open the door to chapter 9.[90]

The definition of municipality in the Code does not include states, and, as such, states cannot file for chapter 9 bankruptcy.[91] Some policy makers have recently suggested that states should be allowed to declare bankruptcy specifically to enable states to manage debt burdens like pension obligations.[92]

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[83] *See, e.g.*, CAL. GOV'T CODE § 53760 (West 2011) (authorizing "any county, city, district, public authority, public agency, or other entity, without limitation, that is a 'municipality,' as defined in [11 U.S.C. § 101(40)], or that qualifies as a debtor under any other federal bankruptcy law applicable to local public entities").

[84] Frederick Tung, *After Orange County: Reforming California Municipal Bankruptcy Law*, 53 HASTINGS L.J. 885, 916–17 (2002).

[85] GA. CODE ANN. § 36-80-5(a) (West 2011) ("No county, municipality, school district, authority, division, instrumentality, political subdivision, or public body corporate created under the Constitution or laws of this state shall be authorized to file a petition for relief from payment of its debts as they mature or a petition for composition of its debts under any federal statute providing for such relief or composition or otherwise to take advantage of any federal statute providing for the adjustment of debts of political subdivisions and public agencies and instrumentalities.").

[86] Tung, *supra* note 84, at 888.

[87] *See* 6 COLLIER ON BANKRUPTCY ¶ 900.LH[6] (Alan N. Resnick & Harry J. Sommer eds., 16th ed. 2011).

[88] 11 U.S.C. § 109(c)(2) (2006).

[89] *In re* Timberon Water & Sanitation Dist., No. 9-07-12142 ML, 2008 WL 5170581, at *2 (Bankr. D.N.M. June 18, 2008) (quoting *In re* Slocum Lake Drainage Dist. of Lake Cnty., 336 B.R. 387, 390 (Bankr. N.D. Ill. 2006)); *see also* Suntrust Bank v. Alleghany-Highlands Econ. Dev. Auth. (*In re* Alleghany-Highlands Econ. Dev. Auth.), 270 B.R. 647, 648–49 (Bankr. W.D. Va. 2001); *In re* Cnty. of Orange, 183 B.R. 594, 604 (Bankr. C.D. Cal. 1995).

[90] *See, e.g.*, Monica Davey, *Michigan Town is Left Pleading for Bankruptcy*, N.Y. TIMES, Dec. 27, 2010, http://www.nytimes.com/2010/12/28/us/28city.html.

[91] 11 U.S.C. § 101(40).

[92] *See* Lisa Lambert, *State Bankruptcy Bill Imminent, Gingrich Says*, REUTERS, Jan. 21, 2011, *available at* http://www.reuters.com/article/2011/01/21/us-usa-states-bankruptcy-idUSTRE70K6PI20110121; *see also*

These proposals, however, have met resistance from state officials who have expressed concern that such an option would increase interest rates in the municipal bond market.[93]

3. Provisions of Chapter 9

Federal law prohibits a bankruptcy court from exercising power that would interfere with any governmental or political powers of the municipality or any property or revenues of the municipality.[94] This limits the court's role in municipal bankruptcy, especially compared to chapter 11 bankruptcies.[95] In municipal bankruptcy, the court does not engage in management of the day-to-day affairs of the municipality, nor is the municipality limited in how it can "use, sell or lease its property."[96]

The immediate benefits to filing a chapter 9 bankruptcy petition are, in many ways, similar to those in chapter 11 bankruptcy.[97] As in chapter 11, a filed petition operates as a stay,[98] prohibiting judgments and actions by creditors under the general provisions of the Code[99] but with limited expansions to the stay for certain tax actions.[100] In general, the creditor's remedies may be more limited when the debtor is a public entity afforded sovereign immunity.[101] However, the stay in bankruptcy affords the municipality relief from any authorized state debt collection methods such as a

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Mary Williams Walsh, *A Path is Sought for States to Escape Their Debt Burdens*, N.Y. TIMES, Jan. 20, 2011, http://www.nytimes.com/2011/01/21/business/economy/21bankruptcy.html.

93 Press Release, National Governor's Association, NGA Statement Regarding Bankruptcy Proposals for States (Jan. 25, 2011) (on file with author), *available at* http://www.nga.org/cms/home/news-room/news-releases/page_2011/col2-content/main-content-list/nga-statement-regarding-bankrupt.html ("The nation's governors strongly oppose federal proposals to provide states with bankruptcy protection. Allowing states to declare bankruptcy is not an authority state leaders have asked for nor would they use. The mere existence of a law allowing states to declare bankruptcy only serves to increase interest rates, raise the costs of state government and create more volatility in financial markets.").

94 11 U.S.C. § 904; 6 COLLIER, *supra* note 87, ¶ 904.01.

95 6 COLLIER, *supra* note 87, ¶ 904.01[1].

96 *Id.* ¶ 904.01[2].

97 Tung, *supra* note 84, at 893–98.

98 11 U.S.C. § 922.

99 *Id.* §§ 362, 901.

100 *Id.* § 922(a); *see also* 6 COLLIER, *supra* note 87, ¶ 922.02[1]–[2] (describing how § 922(a) provides a stay for "actions against an officer or inhabitant of the debtor or against taxes or assessments owed to the debtor" and "attempt[s] to enforce a lien on or 'arising out of' taxes or assessments owed to the debtor").

101 *See, e.g.*, Manders v. Lee, 338 F.3d 1304, 1305 (11th Cir. 2003) (noting that cities and counties do not receive sovereign immunity per se, but they may be entitled to such immunity when acting as an arm of the state).

seizure of municipal bank accounts or a levy on municipal assets,[102] and encourages creditors to negotiate with the governmental entity.[103] In the case of pension debt, this might operate to stay any suit against the municipality to enforce state law obligations to pay pensions.[104]

Chapter 9 does incorporate many of the provisions of chapter 11 that impact the reorganization of debts, including the ability of the debtor to assume or reject executory contracts and unexpired leases.[105] Congress specifically avoided defining the phrase "executory contract," however courts have understood this phrase to mean "contracts on which performance remains due to some extent on both sides."[106] Courts have often relied on the definition promulgated by Professor Countryman[107] which defines an executory contract as "a contract under which the obligation of both the bankrupt and the other party to the contract are so far unperformed that the failure of either to complete performance would constitute a material breach excusing the performance of the other."[108]

Chapter 9 also provides for the debtor to file a plan for the adjustment of its debts.[109] The ability to negotiate a plan of adjustment with creditors[110] is central to municipal bankruptcy.[111] As with chapter 11, a debtor in chapter 9 can "cram down"[112] a plan on unwilling creditors as long as one class of

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102 *See, e.g.*, Silver Sage Partners v. City of Desert Hot Springs (*In re* City of Desert Hot Springs), 339 F.3d 782, 787 (9th Cir. 2003) (issuing a stay limiting judgment creditor from seizing the city's bank accounts and levying against the city's assets).

103 Omer Kimhi, *Reviving Cities: Legal Remedies to Municipal Financial Crises*, 88 B.U. L. REV. 633, 651 (2008).

104 *See* Ferrara, *supra* note 5.

105 11 U.S.C. §§ 365, 901.

106 S. REP. NO. 95-989, at 55 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5787, 5844; H.R. REP. NO. 95-595, at 347 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6303.

107 David G. Heiman, *Executory Contracts, Employee Relations and Pension Claims, Interim Distributions and Acquisition of Interests in Chapter 11 Companies*, *in* CHAPTER 11 BUSINESS REORGANIZATIONS 1991, at 215, 228 (PLI Commercial Law & Practice, Course Handbook Ser. No. 564, 1991).

108 Vern Countryman, *Executory Contracts in Bankruptcy: Part I*, 57 MINN. L. REV. 439, 460 (1972).

109 11 U.S.C. § 941.

110 *Id.* § 943.

111 Tung, *supra* note 84, at 888–89 (basic purpose of municipal bankruptcy is to give a municipality "breathing room" from creditors and to allow them to formulate a repayment plan).

112 The bankruptcy court has the power to "force confirmation of a reorganization plan notwithstanding the dissent of one or more classes of creditors or ownership interests," also known as a "cramdown." 7 COLLIER, *supra* note 87, ¶ 1111.03[1][a][iii]. The plan must be "fair and equitable, with respect to each class of claims or interests that is impaired under, and has not accepted, the plan," and the plan cannot discriminate unfairly. 11 U.S.C. § 1129(b)(1). These provisions help to ensure that the various classes of creditors have

impaired creditors approves the plan.[113] Chapter 9 adopts the chapter 11 requirement for a cramdown that secured creditors receive no less in bankruptcy than the value of their secured claim.[114] However, since there are no shareholders in a municipality, and therefore often no class "junior" to unsecured creditors, these creditors are particularly vulnerable in a cramdown.[115] Even where not explicitly used, the threat of such a measure leads to increased cooperation in bankruptcy, especially from unsecured creditors.[116]

A bankruptcy court must confirm the plan[117] in municipal bankruptcy if the following conditions are met:

> 1. the debtor complies with all of the provisions of the Bankruptcy Code made applicable to a chapter 9 case (*e.g.*, provisions addressing disclosure and solicitation requirements, classification and treatment of claims, good faith requirement);
> 2. the debtor complies with all of the requirements of chapter 9;
> 3. all amounts to be paid by the debtor for services or expenses in the case or incident to the plan are disclosed and are reasonable;
> 4. the debtor is not prohibited by law from taking any action necessary to implement the plan;
> 5. the plan provides for payment in full of all administrative expense claims,[118] unless the holder of such claims agrees to different treatment;
> 6. all regulatory or electoral approval for any action to be taken under the plan has been obtained; and
> 7. the plan is in the best interest of creditors and is feasible.[119]

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balanced leverage in the plan settlement negotiating process. G. Ray Warner, *The Anti-Bankruptcy Act—Revised Article 9 and Bankruptcy*, 9 AM. BANKR. INST. L. REV. 3, 74 (2001). One consequence of the cramdown provisions are that creditors, under the threat of a cramdown, will at times accept reaffirmation or other negotiations at less than the claim amount. Jean Braucher, *Counseling Consumer Debtors to Make Their Own Informed Choices—A Question of Professional Responsibility*, 5 AM. BANKR. INST. L. REV. 165, 180 (1997).

113 11 U.S.C §§ 901(a), 1129(a)–(b).

114 *Id.* §§ 901(a), 1129(b)(2)(A).

115 McConnell & Picker, *supra* note 54, at 464.

116 *See id.*

117 6 COLLIER, *supra* note 87, ¶ 943.03 (noting that 11 U.S.C. § 943 does not mandate that a judge cannot confirm a plan if the conditions in § 943 are not met, but the implication is that the conditions must be met).

118 5 NORTON, *supra* note 52, § 90:20 (explaining that, unlike chapter 11 bankruptcy, the operating expenses of the municipality, such as employee salaries and benefits, are not included in the fifth requirement that the municipality pay administrative expenses).

119 Francisco Vasquez & Eric Daucher, *Restructuring a Municipality Under Chapter 9*, AM. BANKR. INST. J., July–Aug. 2010, at 50, 51.

There are several significant ways in which the conditions for approval of a municipal bankruptcy plan differ from traditional bankruptcy. For example, like in chapter 11, the plan must be "in the best interests of creditors."[120] Under chapter 11, this phrase has been interpreted to mean that the creditors can receive no less than they would if the debtor were liquidated under chapter 7.[121] However, given that liquidation is not an option under chapter 9, legislative history and case law[122] suggest that a plan in chapter 9 meets the "best interest of the creditors" test if the plan is all a creditor can "reasonably expect" in consideration of evidence of the municipality's tax base, its service requirements to the municipality's inhabitants, and the level to which taxes can be raised to fund the plan. [123]

II. PENSION BENEFITS UNDER CHAPTER 11 BANKRUPTCY

Before analyzing the application of current municipal bankruptcy laws to municipal pensions, it is helpful to understand, by way of contrast and comparison,[124] the process by which business entities manage pension debt in a chapter 11 bankruptcy.[125] There are significant differences between federal law's governance of pensions under chapter 11 versus chapter 9. A thorough understanding of chapter 11's processes points to the changes necessary to make chapter 9 a better tool with which to manage pension insolvency.

A. *Intersection of ERISA Law and Chapter 11*

Federal law defines a pension plan as any employer plan that "provides retirement income to employees, or results in a deferral of income by employees for periods extending to the termination of covered employment or

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120 11 U.S.C. § 943(b)(7) (2006).

121 5 NORTON, *supra* note 52, § 90:20.

122 124 CONG. REC. 32,403 (1978) (statement of Rep. Don Edwards) ("The best interest of creditors test does not mean liquidation value as under chapter XI of the Bankruptcy Act. In making such a determination, it is expected that the court will be guided by standards set forth in *Kelley v. Everglades Drainage District*, 319 U.S. 415 (1943) and *Fano v. Newport Heights Irrigation Dist.*, 114 F.2d 563 (9th Cir. 1940), as under present law, the bankruptcy court should make such findings as detailed as possible to support a conclusion that this test has been met.").

123 5 NORTON, *supra* note 52, § 90:20 (internal quotation marks omitted); *accord In re* Corcoran Hosp. Dist., 233 B.R. 449, 453–54 (Bankr. E.D. Cal. 1985) (holding that the chapter 9 plan was in the best interest of creditors where it was based on reasonably anticipated expenses and income).

124 Note, for example, that the Employee Retirement Income Security Act (ERISA) does not apply to governmental entities. 29 U.S.C. § 1003(b)(1).

125 Because there is no liquidation option in a chapter 9 bankruptcy, this comparison will not be made to chapter 7. *See* 11 U.S.C § 901.

beyond."[126] Under this definition, the term "pension" includes "defined benefit plans," which are pension plans other than individual account plans.[127] Defined benefit plans provide a guaranteed payment to the pensioner upon retirement based on an employee's salary and years of employment.[128] A pension is said to "vest" when the employee has completed the minimum amount of time necessary to receive any retirement pay.[129] Importantly, government pension plans are not governed by the Employee Retirement Income Security Act (ERISA).[130]

ERISA was signed into law in 1974 and, among other things, required certain minimum funding levels for pension plans and established public insurance for those plans.[131] The Act was prompted, in part, by the closure of a major auto manufacturing plant whose pension plan was so poorly funded that it left employees without their promised benefits.[132] A pension plan governed by ERISA can only be terminated under the processes set out in ERISA.[133]

Bankruptcy courts have affirmed the provisions in ERISA, reasoning that such laws were the exclusive means of terminating a pension plan, and that they should apply to a debtor's bankruptcy estate as well.[134] ERISA law

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126 29 U.S.C. § 1002(2)(A). ERISA does not govern healthcare benefits, life insurance, or other retirement benefits. *Id.* This paper will not address these employee benefits in the municipal bankruptcy process. These obligations are, however, certainly important factors in municipal debt. *See* John Ouellette, *Panel, Reports Call for Health and Pension Reforms*, MASS. MUN. ASSOC. (May 7, 2010), http://www.mma.org/local-aid-and-finance/4611-panel-reports-call-for-health-and-pension-reforms (citing cities' rising health care expenditures and the need for reform). However, state laws guaranteeing public pension benefits do not usually extend to other retirement benefits, and municipalities can modify these benefits, even for vested retirees, without the same legal restrictions. *See, e.g.*, Lippman v. Bd. of Educ., 487 N.E.2d 897, 898 (N.Y. 1985) (holding that Article V, Section 7 of the New York Constitution, which protects pension benefits as contractual rights, does not extend to health insurance benefits). Additionally, these other retirement benefits are treated differently than pensions under bankruptcy law. *See* 11 U.S.C. § 1114(a).

127 29 U.S.C. § 1002(35).

128 Daniel Keating, *Chapter 11's New Ten-Ton Monster: The PBGC and Bankruptcy*, 77 MINN. L. REV. 803, 805 (1993).

129 Deering v. Deering, 437 A.2d 883, 885 n.3 (Md. 1981).

130 29 U.S.C. § 1003(b)(1).

131 Andrew Stumpff, *Darkness at Noon: Judicial Interpretations May Have Made Things Worse For Benefit Plan Participants Under ERISA Than Had the Statute Never Been Enacted, in* ERISA LITIGATION 2010, at 249, 257 (PLI Litigation & Admin. Practice, Handbook Ser. No. 831, 2010).

132 *Id.* (citing JAMES A. WOOTEN, THE EMPLOYEE RETIREMENT INCOME SECURITY ACT OF 1974: A POLITICAL HISTORY 51–79 (2004)).

133 29 U.S.C. § 1341(a)(1).

134 *See In re* Phillip Servs. Corp., 310 B.R. 802, 809 (Bankr. S.D. Tex. 2004) (stating that, in a bankruptcy case, "[t]he statute starts with the statement that the ERISA termination provisions are the [e]xclusive means of plan termination"); *see also* Pension Benefit Guar. Corp. v. Pritchard (*In re* Esco Mfg. Co.), 50 F.3d 315, 316 (5th Cir. 1995) (noting that Congress intended ERISA to "provide the sole and exclusive means under which a

provides a structure for termination of a pension in bankruptcy that, among other procedural protections, requires the bankruptcy court to approve the termination and determine that "unless the plan is terminated, [the debtor] will be unable to pay all its debts pursuant to a plan of reorganization and will be unable to continue in business outside the chapter 11 reorganization process."[135]

Courts have held that ERISA's reference to "'a' plan of reorganization" does not mean that any plan of reorganization that includes a pension termination provision is therefore permitted.[136] "[R]ather the test is whether the debtor can obtain confirmation of *any* plan of reorganization without termination of the retirement plan. The burden of proof for a distress termination is on the sponsor of the plan."[137] For example, a bankruptcy court held termination necessary under this standard when it found that a company that filed for bankruptcy needed to increase profits by 70% in the subsequent six months to pay for pension obligations, a goal that the court determined was "impossible under current industry conditions."[138]

If a business terminates a pension plan in bankruptcy under ERISA, the protections of the Pension Benefit Guaranty Corporation (PBGC) apply.[139] The PBGC was created to "protect employees against the loss of 'nonforfeitable' benefits upon termination of pension plans lacking sufficient funds to pay benefits in full."[140] The PBGC is funded first by the assets of the terminated pension plan[141] and then by premiums paid by the insured companies.[142] The PBGC guarantees a certain percentage of monthly benefits if the plan is terminated,[143] subject to certain limitations.[144] The maximum premium that the

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qualified pension plan may be terminated" (quoting H.R. Rep. No. 99-300, at 289 (1985), *reprinted in* 1986 U.S.C.C.A.N. 756, 940)).

135 29 U.S.C. § 1341(c)(2)(B)(ii)(IV).

136 *In re* U.S. Airways Grp., Inc., 296 B.R. 734, 743–44 (Bankr. E.D. Va. 2003).

137 *Id.* at 744 (citation omitted).

138 *In re* Sewell Mfg. Co., 195 B.R. 180, 186 (Bankr. N.D. Ga. 1996).

139 29 U.S.C. § 1322(a).

140 Raymond B. Yates, M.D., P.C. Profit Sharing Plan v. Hendon, 541 U.S. 1, 7 (2004).

141 29 U.S.C. § 1344.

142 *Id.* § 1306(a); *see* Nicholas J. Brannick, *At the Crossroads of Three Codes: How Employers Are Using ERISA, the Tax Code, and Bankruptcy to Evade Their Pension Obligations*, 65 OHIO ST. L.J. 1577, 1581–82 (2004).

143 29 U.S.C. §§ 1322–1323.

144 *See, e.g.*, *id*. § 1322(b)(1) (providing that no benefits provided or increased within five years of the plan termination are covered by the PBGC).

PBGC will insure is set annually, and for 2010 was capped at $54,000 a year for those who retire at age sixty-five.[145]

In the case of termination through a bankruptcy proceeding, the PBGC may participate in a chapter 11 bankruptcy as a creditor for claims on both the amount of any underfunding as well as any unpaid contributions.[146] Because pension benefits are paid only upon retirement and only if the pensioner is vested, and because they continue to be paid until the pensioner's death, the value of PBGC's claim rests on a number of actuarial assumptions including the life expectancy of the plan's recipients.[147] In addition to this valuation, the court must determine the present value of the claim by calculating the discount rate for such a claim.[148] This reflects the "economic reality that a certain amount of money received today is worth more than the same amount of money received tomorrow."[149]

B. Priority of Pension Expenses

Chapter 11 provides that payments for retiree benefits such as health and life insurance are administrative expenses[150] and should be paid in cash to those owed on the effective date of the plan of reorganization unless there is an agreement otherwise.[151] Chapter 11 contains no such explicit provision for pensions, however. The general provisions of the Code require that administrative expenses be "actual" and "necessary" and that they include only wages, salaries, and commissions for services rendered after the commencement of the case, among other expenses.[152] Courts have evaluated whether an expense is actual and necessary under a two part test inquiring whether the expense: "(1) . . . arose from a transaction with the bankruptcy

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145 The PBGC guarantees a lesser amount for those who retire at a younger age and a higher amount for those who retire at an older age. Press Release, Pension Benefit Guar. Corp., PBGC Announces Maximum Ins. Benefit for 2010 (Oct. 27, 2009), *available at* http://www.pbgc.gov/ news/ press/ releases/pr10-02.html.

146 *See, e.g.*, *In re* Kaiser Aluminum Corp., 456 F.3d 328, 330 (3d Cir. 2006); *see also In re* Kent Plastic Corp., 183 B.R. 841, 844 (Bankr. S.D. Ind. 1995); *In re* Columbia Packing Co., 47 B.R. 126, 128 (Bankr. D. Mass. 1985). This does not mean that the PBGC is eligible, however, to pursue in bankruptcy proceedings the $1250 per plan member termination premium that employers are required to pay for three years after certain terminations. *See* 29 U.S.C. § 1306(a)(7)(A). The Second Circuit has held that these termination premiums are not prepetition claims. Pension Benefit Guar. Corp. v. Oneida Ltd., 562 F.3d 154, 158 (2d Cir. 2009).

147 Daniel Keating, *supra* note 128, at 818.

148 2 NORTON, *supra* note 52, § 48.11.

149 *In re* Lowen Grp. Int'l, Inc., 274 B.R. 427, 434 (Bankr. D. Del. 2002).

150 11 U.S.C. § 1114(e)(2) (2006).

151 *Id.* § 1129(a)(9).

152 *Id.* § 503(b)(1)(a).

estate and (2) . . . directly and substantially benefitted the estate."[153] Courts have held that obligations for pension plan contributions for work performed prepetition, even if they are due postpetition, could not be treated as an administrative priority.[154] Therefore, claims for pension contributions either (a) owed prior to the filing of the bankruptcy petition or (b) owed after the filing for work performed prior to the filing are typically treated as general unsecured claims.[155] Presumably, pension obligations due after the filing of the bankruptcy for work also performed after the filing of the bankruptcy would be an allowable administrative expense.

C. Collective Bargaining Protections in Chapter 11

Pensions that are included in a collective bargaining agreement are subject to further procedural protections under the Code.[156] The Supreme Court in *National Labor Relations Board v. Bildisco & Bidisco* held that a debtor in possession could reject a collective bargaining agreement only if the "equities balance in favor of [rejection]"[157] but that such rejection could take place unilaterally without the otherwise required collective bargaining.[158] The Supreme Court reasoned that the special nature of collective bargaining agreements required the Court to impose a stricter test than the "business judgment test" usually used in rejecting executory contracts.[159]

While the Supreme Court in *Bildisco* resolved a conflict among the circuits,[160] this holding sparked debate in Congress, and within five months of the Court's decision, Congress passed an amendment to the Code.[161] The new § 1113 provided prerequisites for the rejection of collective bargaining

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153 McMillan v. LTV Steel, Inc. 555 F.3d 218, 226 (6th Cir. 2009) (quoting *In re* Eagle-Picher Indus., Inc., 447 F.3d 461, 464 (6th Cir. 2006)) (internal quotation marks omitted).

154 *In re* A.C.E. Elevator Co., Inc., 347 B.R. 473, 480 (Bankr. S.D.N.Y. 2006) (citing *In re* Finley, Kumble, 160 B.R. 882, 887–91 (Bankr. S.D.N.Y. 1993)).

155 11 U.S.C. § 507.

156 *Id*. § 1113.

157 NLRB v. Bildisco & Bildisco, 465 U.S. 513, 526 (1984), *partially superseded by statute*, Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, 98 Stat. 376.

158 *See* Truck Drivers Local 807 v. Carey Transp. Inc, 816 F. 2d 82, 87 (2d Cir. 1987) (citing *Bildisco*, 465 U.S. at 534).

159 *Bildisco*, 465 U.S. at 524.

160 *See In re* Carey Transp., Inc., 50 B.R. 203, 205 (Bankr. S.D.N.Y. 1985).

161 Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, § 541(a), 98 Stat. 376, 390; *see also* 11 U.S.C. § 1113 (the Code section that Congress enacted in response to *Bildisco*); Century Brass Prods., Inc. v. UAW Local 1604 (*In re* Century Brass Prods., Inc.), 795 F.2d 265, 273 (2d Cir. 1986) (describing the passage of 11 U.S.C. § 1113).

agreements and established standards a judge should use in granting the rejection of such agreements.[162] Under this revision, a debtor in possession must make a submission to the union proposing the modification of benefits and provide the information necessary for the union to evaluate the proposal prior to seeking rejection of the collective bargaining agreement with the court.[163] Such modifications must be "necessary to permit the reorganization" and must assure that "all creditors, the debtor and all of the affected parties are treated fairly and equitably."[164] Thereafter, the trustee must negotiate in good faith with the union.[165] The court will not approve the debtor's rejection of the collective bargaining agreement unless and until the court determines that the union has failed to accept the debtor's proposal without good cause and that "the balance of the equities clearly favors rejection of such an agreement."[166]

Courts have adopted conflicting opinions on the necessity that justifies the rejection of the collective bargaining agreement.[167] Some courts have interpreted "necessity" to mean "essential" to the reorganization.[168] Others have interpreted "'necessity'" as placing on the debtor the "burden of proving that its proposal is made in good faith, and that it contains necessary, but not absolutely minimal, changes that will enable the debtor to complete the reorganization process successfully."[169] Several have argued these two interpretations have become indistinguishable, and for practical purposes, those courts have applied § 1113 with the lower threshold.[170] While § 1113 may appear pro-debtor on its face, research conducted after the passage of § 1113 suggests that these provisions are in fact more favorable to unions than the standards implemented in *Bildisco*.[171]

One might debate whether the standards for termination under the Code are significantly different from the standards the Supreme Court laid out in

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162 11 U.S.C. § 1113; 5 NORTON, *supra* note 52, § 104:6.
163 11 U.S.C. § 1113(b)(1).
164 *Id*.
165 *Id*. § 1113(b)(2).
166 *Id.* § 1113(c).
167 *See* Truck Drivers Local 807 v. Carey Transp. Inc, 816 F.2d 82, 88–89 (2d Cir. 1987).
168 *See id.* at 89 (citing Wheeling-Pittsburgh Steel Corp. v. United Steelworkers, 791 F.2d 1074, 1088 (3d Cir. 1986)).
169 *See id.* at 90.
170 *See* Andrew B. Dawson, *Collective Bargaining Agreements in Corporate Reorganizations*, 84 AM. BANKR. L.J. 103, 113 (2010).
171 A study showed debtors were able to reject their collective bargaining agreements in 58% of all cases between 1984 and 1993, after the passage of § 1113, compared to 67% of the cases prior to 1984, suggesting that the protections in § 1113 provided a real, though perhaps modest, impact. *See id*.

Bildisco;[172] however, the process for rejection under the Code[173] is certainly more stringent.[174] In addition to carefully delineated bargaining requirements,[175] § 1113 also requires an expedited time frame for review, including a hearing within fourteen days after the debtor files an application to reject a collective bargaining agreement[176] and a ruling by the court thirty days thereafter.[177]

The insurance of pensions through the PBGC, the regulation of pensions under ERISA,[178] and the collective bargaining and prioritization provisions in chapter 11[179] are examples of federal law setting protections for pensioners and processes through which employers manage pension obligations. Since chapter 11 and ERISA do not apply to government pension plans, one must look to state pension laws and chapter 9 to determine what protections and processes are available for government pensioners and municipalities.

III. STATE LAW PENSION PROTECTIONS

A. State Pension Laws

State laws protecting pensions[180] are the biggest limitations to a municipality reducing or avoiding existing pension obligations. Because ERISA does not apply to governmental pension plans,[181] they are subject only to state regulations on funding[182] and structure.[183]

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[172] *Compare* 11 U.S.C. § 1113(c)(3) (2006) (stating that the court must consider "the balance of the equities"), *with* NLRB v. Bildisco & Bildisco, 465 U.S. 513, 526 (1984) ("[T]he Bankruptcy Court should permit rejection of a collective-bargaining agreement . . . if the debtor can show that the collective-bargaining agreement burdens the estate, and that after careful scrutiny, the equities balance in favor of rejecting the labor contract."), *partially superseded by statute*, Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, 98 Stat. 376.

[173] 11 U.S.C. § 1113.

[174] Omer Kimhi, *Chapter 9 of the Bankruptcy Code: A Solution in Search of a Problem*, 27 YALE J. ON REG. 351, 358 (2010) ("The *Bildisco* decision offers a relatively lenient standard for the rejection of CBAs, because as opposed to [§] 1113, under *Bildisco* the court does not need to inject itself into the negotiations and evaluate the reasonableness of the debtor's proposals.").

[175] 11 U.S.C. § 1113(b)(1), (c)(1)–(2).

[176] *Id.* § 1113(d)(1).

[177] *Id.* § 1113(d)(2).

[178] Stumpff, *supra* note 131, at 249, 257.

[179] 11 U.S.C. § 1113.

[180] *See, e.g.*, Navlet v. Port of Seattle, 194 P.3d 221, 232 (Wash. 2008) (en banc).

[181] 29 U.S.C. § 1003(b)(1).

[182] *See, e.g.*, 53 PA. STAT. ANN. §§ 895.302(c), 895.303(c) (West 2011).

[183] *See, e.g.*, CAL. GOV'T CODE § 7507.5 (West 2011).

Municipal governments fund employee pensions in a number of ways. In many instances, municipalities contribute to a pension trust fund that is responsible for both investing the money and paying claims.[184] Sometimes this trust fund is pooled with other municipal employers or with the state.[185] Alternatively, because the requirement for nongovernmental entities to utilize pension trusts under ERISA does not apply to municipalities, [186] the pension obligations may be paid directly to pensioners by municipalities from their general budget on a "pay-as-you-go" basis.[187]

Most state laws set strict statutory and constitutional limits on changes to or reductions of pension benefits.[188] There are several general models for such restrictions.[189] In many states, a vested public pension is viewed as a contractual right.[190] Under this model, there are state due process concerns with modifying pension obligations,[191] and pensions can only be altered under a state and federal constitutional Contracts Clause analysis.[192] Additionally, several states that view a pension as a contractual right, including California, allow changes to the pension plan only if any reductions can be offset by a new benefit of equal or greater value.[193] This is the so-called "California rule." [194]

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184 *See, e.g.*, PITTSBURGH, PA., CODE ORDINANCES tit. 1, art. IX, ch. 176 (1986).

185 *See, e.g.*, Objection by California Public Employees' Retirement System of the City of Vallejo's Motion for Approval of Rejection of Collective Bargaining Agreements at 2, *In re* City of Vallejo, 403 B.R. 72 (Bankr. E.D. Cal. 2009) (No. 08-26813-A-9) (noting that the City of Vallejo contributed to a state-wide retirement system for their municipal employees).

186 29 U.S.C. § 1103.

187 Jonathan Barry Forman, *Funding Public Pension Plans*, 42 J. MARSHALL L. REV. 837, 841–42 (2009) (explaining that, though ERISA does not apply to local government pensions and the laws allow for "pay-as-you-go" plans, accounting standards set for municipalities by the Government Accounting Standards Board (GASB) have made many municipalities pre-fund pension obligations, though likely less than 100% funding).

188 3 EUGENE MCQUILLIN, THE LAW OF MUNICIPAL CORPORATIONS § 12.141 (3d ed. 1978).

189 *See, e.g.*, Marvel v. Dannemann, 490 F. Supp. 170, 173 (D. Del. 1980) (holding that pension was a contractual right); *see also* State v. McMillan, 319 S.E.2d 1, 7 (Ga. 1984) (holding that pension was a property right); Maffei v. Sacramento Cnty. Employees' Ret. Sys., 127 Cal. Rptr. 2d 279, 284 (Cal. Ct. App. 2002) (holding reductions in pension plan benefits must be offset by comparable benefits).

190 *See, e.g.*, *Marvel*, 490 F. Supp. at 173; Fund Manager, Pub. Safety Pers. Ret. Sys. v. City of Phx. Police Dep't Pub. Safety Pers. Ret. Sys. Bd., 728 P.2d 1237, 1239, 1241 (Ariz. Ct. App. 1986).

191 *See, e.g.*, Cal. Ass'n of Prof'l Scientists v. Schwarzenegger, 40 Cal. Rptr. 3d 354, 361 n.5 (Cal. Ct. App. 2006) ("The [C]ontract [C]lause of the federal Constitution (art. I, § 10) prohibits any state from passing a law 'impairing the obligations of contracts.' . . . The California Constitution similarly provides that '[a] . . . law impairing the obligation of contracts may not be passed.'" (citation omitted) (quoting CAL. CONST. art. I, § 9; Lyon v. Flournoy, 76 Cal. Rptr. 869, 873 (Cal. Ct. App. 1969))).

192 *See, e.g.*, *Fund Manager, Pub. Safety Pers. Ret. Sys.*, 728 P.2d at 1240 (evaluating whether a change in an accidental disability pension benefit was legal and holding "[t]he state's power to modify contracts is limited, however, by the [C]ontract [C]lause of the Arizona Constitution and the United States Constitution").

193 *See, e.g.*, *Maffei*, 127 Cal. Rptr. 2d at 284; Olson v. Cory, 636 P.2d 532, 541 (Cal. 1980).

In other states, such as Georgia, a pension is viewed as a property interest of the pensioner, and such interest cannot be reduced without due process.[195] In still other states, such as Michigan, rights of pension members are explicitly protected in the state constitution.[196] This constitutional protection usually bars the public employer from reducing or modifying the benefits of pension members other than for prospective members.[197]

Many state laws prohibit changing a pension benefit for any worker that has completed any portion of service (i.e., for anyone other than newly hired employees).[198] Under Georgia law, for example, even if the employee is not technically vested in the retirement plan, his or her rights to the retirement plan are "constitutionally vested."[199] This means that, if a pension plan in Georgia requires fifteen years of service for the pensioner to vest in the pension plan and thus to be eligible to retire with some portion of the promised pension benefits, a pensioner with less than fifteen years would nonetheless still be protected from any amendments to the pension plan that would reduce the employee's pension benefits even prior to completion of the fifteen-year term of service.[200]

B. State Labor Laws

The National Labor Relations Act (NLRA) governs organized labor in the United States, but it does not apply to government employers.[201] Therefore, the state law governing labor relations is the binding law for municipal

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194 *See* Betts v. Bd. of Admin., 582 P.2d 614, 617 (Cal. 1978); *see also* Jeffery B. Ellman & Daniel J. Merrett, *Pensions and Chapter 9: Can Municipalities Use Bankruptcy to Solve Their Pension Woes?*, 27 EMORY BANKR. DEV. J. 365, 380–81 (2011).

195 *See* State v. McMillan, 319 S.E.2d 1, 7 (Ga. 1984); *see also In re* Disciplinary Proceedings Against Erickson, 556 N.W.2d 99 (Wis. 1996); Pineman v. Oechslin, 488 A.2d 803, 808–09 (Conn. 1985); Withers v. Register, 269 S.E.2d 431, 432–33 (Ga. 1980).

196 MICH. CONST. art. IX, § 24 ("The accrued financial benefits of each pension plan and retirement system of the state and its political subdivisions shall be a contractual obligation thereof which shall not be diminished or impaired thereby."); *see also* ALASKA CONST. art. XII, § 7; 60 AM. JUR. 2D *Pensions* § 1176 (2003).

197 *See Withers*, 269 S.E.2d at 432–33.

198 *See, e.g.*, *id*. ("[I]f the employee contributes at any time any amount toward the benefits he is to receive, and if the employee performs services while the law is in effect; and that the impairment clause of our constitution (Art. I, Sec. I, Par. VII, Constitution of Georgia of 1976; Code Ann. § 2-107) precludes the application of an amendatory statute or ordinance in the calculation of the employee's retirement benefits if the effect of the amendment is to reduce rather than increase the benefits payable.")

199 *See id.*

200 *See id.*

201 29 U.S.C. § 152(2) (2006).

employers.[202] In states that have municipal workers unions, the provision of pension benefits for active employees or the contributions required for pension trusts, as well as contributions for retirees,[203] are typically included in collective bargaining agreements.[204]

IV. CURRENT SOLUTIONS FOR THE MUNICIPAL PENSION PROBLEM

A. State-Authorized Local Tools

A municipality that is having difficulty meeting its pension obligations, or that is having difficulty paying its operating expenses because of the obligations from its pensions, has few options given the pension rights of both current and retired employees.[205] Even under the most restrictive of state law schemes, however, municipalities are able to change pension benefits for employees hired in the future.[206] In fact, many state and local governments have responded to pension pressures in recent years by changing the terms of retirement benefits for newly hired employees.[207] This can and has been done by raising the retirement age, reducing benefits, or converting wholesale into a defined contribution[208] or a 401(k)-like plan, but such changes are only applicable to new prospective employees.[209] However, because the payouts for

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202 *See, e.g.*, Public Employment Relations Act, ALASKA STAT. § 23.40.070–.260 (West 2011); *see also* MICH. COMP. LAWS ANN. §§ 423.201–.216 (West 2011); OR. REV. STAT. ANN. § 243.650 (West 2011).

203 *See, e.g.*, Rabinowitz v. City of Hartford, No. CV075008403S, 2010 WL 4075425, at *1 (Conn. Super. Ct. Sept. 30, 2010) (involving action by retirees against the city for the proper payment of retiree pensions according to the provisions of the collective bargaining agreement).

204 *See, e.g.*, Navlet v. Port of Seattle, 194 P.3d 221, 225 (Wash. 2008) (en banc) (describing the collective bargaining terms that require the union to contribute into the pension trust).

205 *See, e.g.*, *id.* at 232 (citing Abels v. Snohomish Cnty. Pub. Util. Dist. No. 1, 849 P.2d 1258 (1993)); *see also* Police Pension Fund Ass'n Bd. v. Hess, 562 A.2d 391 (Pa. 1989).

206 *See* Withers v. Register, 269 S.E.2d 431, 432–33 (Ga. 1980).

207 *See, e.g.* Alicia Robinson, *RIVERSIDE: Lower Pension Tier Formalized*, PRESS ENTERPRISE, Sept. 22, 2011, http://www.pe.com/local-news/riverside-county/riverside/riverside-headlines-index/20110923-riverside-lower-pension-tier-formalized.ece (reporting increases in pension contributions and decreases in pension benefits for new hires); *see also* Randall Jensen, *San Diego Ahead in Pension Reform*, BOND BUYER, Jan. 7, 2011, http://www.bondbuyer.com/issues/120_5/san_diego_pension-1021855-1.html (explaining how San Diego has decreased pension benefits for new hires).

208 70 C.J.S. *Pensions* § 24 (2005) ("An individual account plan or defined contribution plan is a pension plan which provides for an individual account for each participant and for benefits based solely upon the amount contributed to the participant's account, and any income, expenses, gains, and losses and any forfeitures of other participants which may be allocated to the account.").

209 *See* RONALD SNELL, NAT'L CONF. ST. LEGISLATURES, STATE RETIREMENT SYSTEM DEFINED CONTRIBUTION PLANS 3–4 (2009), *available at* http://www.ncsl.org/Portals/1/Documents/employ/StateGovtDCPlansSept2009.pdf.

the pensions or other retirement benefits of the newly-hired stretch decades into the future, these changes do not significantly aid municipal governments in their ability to deal with pension obligations and debt more immediately owed.

A municipality overly burdened by pension obligations, yet obligated under state law to pay these obligations, can respond in a variety of ways depending on the financial status of its annual budget and the financial health of its pension fund.[210] Generally, municipalities would be required to pay out of general funds when pension trust funding is insufficient to pay claims[211] or meet defined trust or state minimum funding levels.[212] Where authorized by state law, a municipality might also sell pension bonds to pay for the liability.[213] As an increasing portion of a municipality's operating budget goes towards funding pension obligations, this can frustrate the municipality's ability to meet its municipal service mandates and to make payments for other debt obligations.[214]

A municipality with a distressed budget might be unable to make payments out of general funds as political pressures could keep it from dedicating general tax revenues to pension obligations. In certain instances, when a pension trust has available funds, local governments have liquidated pension trust fund assets or reserves to pay their more immediate pension

[210] *See, e.g.*, Kenneth Lowe, *Decatur Public Library Continues to Feel Squeeze of Tight Budget*, HERALD-REVIEW, Dec. 16, 2010, http://www.herald-review.com/news/local/article_2eb4df60-fbd7-5e96-b646-9d3fd84130b1.html (describing how the city enacted deep cuts to public library to fund increasing pension costs); Michael McDonald & Adam L. Cataldo, *'Dumbest Idea Ever' Used as Pensions Plug Deficit (Update 2)*, BLOOMBERG, May 1, 2008, http://www.bloomberg.com/apps/news?pid=newsarchive&sid=arYeVtZeBd4s (stating that Philadelphia Mayor Edward Rendell sold $1.29 billion in pension bonds in 1999 and a later governor then stopped making contributions to the pension fund to balance the budget).

[211] *See, e.g.*, Westly v. Cal. Pub. Emps. Ret. Sys. Bd. of Admin., 130 Cal. Rptr. 2d 149, 155 n.7 (Cal. Ct. App. 2003) (noting that provisions protecting the state pension fund were passed in part to protect tax increases which would result if funds were mismanaged).

[212] *See, e.g.*, Municipal Pension Plan Funding Standard and Recovery Act, 53 PA. CONS. STAT. §§ 895.101–.1131 (2009).

[213] *See, e.g.*, Mary Williams Walsh & Michael Cooper, *Illinois Pension Bonds to Test Investors' Faith*, N.Y. TIMES, Feb. 18, 2011, http://www.nytimes.com/2011/02/18/business/18illinois.html ("Illinois hopes to sell $3.7 billion of bonds to make this year's contribution to its fund. It is essentially paying a single year's bill by adding to its already heavy debt load."); Spadoro v. Whitman, 695 A.2d 654, 655 (N.J. 1997) (upholding the constitutionality of New Jersey's Pension Bond Financing Act of 1997).

[214] *See, e.g.*, Tom Barrett, Mayor, City of Milwaukee, Proposed Executive Budget Speech, p. 2–3 (Sept. 23, 2010) *available at* http://www.ci.mil.wi.us/ImageLibrary/Groups/MayorAuthors/2010/budget/1009232010BudgetAddress.pdf (announcing his intention to pay the $49 million pension obligation out of general funds, which required that the city cut more than $31 million in operating spending and that the city eliminate 360 full-time equivalent positions).

obligations.[215] In Chicago, Illinois, for example, where unfunded pension liabilities were estimated to be $41,966 per city household,[216] city officials announced a plan to sell pension assets to meet the city's 2010 pension obligations.[217] While asset liquidation is certainly a short-term solution to fund current pension obligations, unless the trust assets can sustain a municipality until revenues increase or expenses decrease (for example, until the benefits of pension changes for newly hired employees are reaped by the municipality), the effectiveness of this strategy is likely to be short-lived. Ultimately, a municipality might be required to draw from general funds in the future if the pension assets fall short.

As an alternative to selling pension assets, or as a strategy used in conjunction with selling pension assets, a state may increase the contributions of current employees to pay for retiree expenses.[218] This "pay-as-you-go" model emulates the Federal Government's Social Security program, where deductions from the paychecks of today's workers are paying for the benefits of today's retirees.[219] However, this funding strategy in the Social Security program has been criticized in derisive language as a "giant Ponzi scheme."[220] Such a strategy for pension funding is also likely to be short sighted because the contributions from current employees will likely not keep pace with growing retiree obligations.[221] Moreover, this strategy may result in political pressure from current employees who are disproportionately required to bear the costs of pension obligations while simultaneously having reason to doubt the viability of the pension trust for their own long-term benefits.

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215 *Illinois, Kentucky Forced to Sell Off Pension Assets*, INSTITUTIONAL INVESTOR, Oct. 7, 2010, http://www.institutionalinvestor.com/pensions_and_endowments/Articles/2683814/Illinois-Kentucky-Forced-To-Sell-Off-Pension-Assets.html.

216 *Dire Outcomes Predicted for Municipal Pension Systems*, KELLOGG SCHOOL OF MANAGEMENT, Oct. 10, 2010, http://www.kellogg.northwestern.edu/News_Articles/2010/municipal-pension-systems.aspx (last visited Jan. 4, 2011).

217 *See, e.g.*, Dardick, *supra* note 45.

218 *See, e.g.*, Jeff Sistrunk & Katie Brenzel, *Tax Relief from Pension Reform? Towns Wait and See*, NJ HERALD, October 8, 2011, http://www.njherald.com/story/news/PENSIONREFORM-1011-web (noting that the town increased employee pension contributions by up to 1.5% of employee's salaries to net a $145,000 reduction in city pension contributions).

219 Gary Burtless, *Income and Social Security and Substandard Working Conditions*, 51 INDUS. & LAB. REL. REV. 528, 529 (1998).

220 *See* Jerry W. Markham, *Privatizing Social Security*, 38 SAN DIEGO L. REV. 747, 756 n.48 (2001).

221 Burtless, *supra* note 219, at 529 (arguing that increased life spans and decreased fertility rates will impact "pay-as-you-go" pension solvency just as it has in Social Security).

This toolbox for managing pension obligations has been, and will likely continue to be, sufficient to keep most municipalities current on their debt obligations.[222] However, a municipality that is facing a shrinking tax base or the fallout from poor municipal investments,[223] and growing pension debts, may have its ability to provide basic municipal services threatened by its need to pay debt obligations or simply be unable to pay debts. Some states allow for a process of state court receivership or some comparable alternative in the case of an insolvent municipality.[224] Additionally, in practice, many states have come to the financial aid of municipalities teetering on the verge of bankruptcy, choosing to spend state dollars rather than allowing municipal bond defaults within their borders.[225]

B. A State-Authorized Federal Solution: Chapter 9

A municipality's financial burdens may limit the effectiveness of these tools, and a state may be unable or unwilling to "bail out" these local governments. In many states, the same factors that have led to municipal insolvency—reduction in both tax revenues and federal aid coupled with increased legacy obligations—have also put states in a precarious position.[226] Even in states that are able to come to the aid of municipalities, there might be

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[222] This is evidenced by the fact that there have been only roughly forty general-purpose municipal bankruptcy filings from 1976 to January 2009. Kimhi, *supra* note 174, at 359.

[223] *See, e.g.*, Cnty. of Orange v. Merrill Lynch & Co. (*In re* Cnty. of Orange), 241 B.R. 212, 214 (Bankr. C.D. Cal. 1999) ("In 1994, Orange County, California, filed the largest municipal bankruptcy in history after failure of a risky leveraged investment scheme by its Treasurer.").

[224] Forrest, *supra* note at 83 (citing R.I. GEN. LAWS § 45-9-1 (West 2011)) (discussing a Rhode Island state law that requires a fiscal overseer and other requirements in the case of a municipal fiscal emergency).

[225] *See, e.g.*, Press Release, Pennsylvania Office of the Governor, Commonwealth Partnering With City of Harrisburg To Help It Meet Immediate Financial Obligations (Sept. 12, 2010) (on file with author) (announcing that the State of Pennsylvania would provide $4.3 million in economic assistance to the city of Harrisburg to help the city pay an upcoming bond payment as well as pay for a financial management firm to craft a plan to help the city out of debt after previously announcing that they would be unable to make a general obligation bond payments).

[226] NAT'L GOVERNORS ASS'N, ISSUE BRIEF: STATE GOVERNMENT REDESIGN EFFORTS 2009 AND 2010 (2010) (reporting "record budget shortfalls over the past several years," with fiscal year 2010 expenditures down to $612.9 billion from $687.3 billion in fiscal year 2008 and that states have implemented many budget cuts and programmatic changes adjusting to what may be "the new normal").

a resistance to do so for fear of the "moral hazard"[227] inherent in such an action.[228]

There are thus limited choices to manage municipal pension debt under state regimes. Many of the federal law "protections" for employee benefits and compensation (e.g., ERISA, NLRA) defer to state law for governmental entities,[229] and many state and municipal laws restrict modification or termination of pension benefits[230] and unilateral modification of labor agreements in states with public labor unions.[231] However, federal bankruptcy law, where authorized by state law,[232] gives a municipality tools they would not traditionally have under the above-mentioned state law and constitutional limitations.[233]

Few municipalities to date have utilized chapter 9 to terminate a pension trust or modify existing pension obligations,[234] but the definitions in the Code would certainly accommodate the inclusion of such debt.[235] The Code defines the term "claim" as a "right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured."[236] This broad definition would likely encompass pension obligations owed to pensioners and would give the pensioners standing like any creditor.[237]

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227 OFFICE OF THE SPECIAL INSPECTOR GEN. FOR THE TROUBLED ASSET RELIEF PROGRAM, SIG-GR-09-04, QUARTERLY REPORT TO CONGRESS 3 (2009), *available at* http://www.sigtarp.gov/reports/congress/2009/October2009_Quarterly_Report_to_Congress.pdf (defining moral hazard as "the lack of incentive individuals have to guard against a risk when they are protected against that risk").

228 Similar arguments were made regarding the government's bailout of AIG and GM. *See, e.g.*, Ann Graham, *Bringing to Heel the Elephants in the Economy: The Case For Ending "Too Big To Fail,"* 8 PIERCE L. REV. 117, 151 (2010) ("[I]t is the expectation of continued government bailouts that creates the most serious cases of moral hazard and distorted resource allocation.").

229 *See* 29 U.S.C. § 1003(b)(1); *see also id.* § 152(2).

230 *See* ALASKA CONST. art. XII, § 7; MICH. CONST. art. IX, § 24 ("The accrued financial benefits of each pension plan and retirement system of the state and its political subdivisions shall be a contractual obligation thereof which shall not be diminished or impaired thereby."); Withers v. Register, 269 S.E.2d 431, 432 (Ga. 1980); *Pensions*, *supra* note 196, § 1176.

231 *See, e.g.*, CAL. GOV'T CODE § 3515.7 (West 2011); City of Vallejo Charter, art. 7, § 809.

232 11 U.S.C. § 109(c).

233 *See* Louisville Joint Stock Land Bank v. Radford, 295 U.S. 555, 589 (1935) ("[U]nder the bankruptcy power Congress may discharge the debtor's personal obligation, because, unlike the states, it is not prohibited from impairing the obligations of contracts.").

234 *See* Ellman & Merrett, *supra* note 194, at 411.

235 11 U.S.C. § 101(5)(a).

236 *Id.*

237 *Id.* § 943 (stating the requirements for plan confirmation in chapter 9).

1. The Insolvency Requirement

The Code insolvency requirement serves as a "gatekeeper" by discouraging superfluous filings.[238] The Code defines municipal insolvency in two ways: "(i) generally not paying . . . debts as they become due unless such debts are the subject of a bona fide dispute; or (ii) unable to pay . . . debts as they become due." [239] A mere budget deficit would probably not be sufficient to meet these criteria,[240] but instead the court would likely conduct a cash flow analysis to determine if debts could be paid as they come due.[241] As part of this analysis, the court might look to see if there are available cash reserves.[242] In *In re Bridgeport*, the court held that the city did not meet the definition of insolvency because the city had not drawn down monies from a contingency fund that would enable the city, if spent, to meet its budget for that year.[243]

It is important to note that bond defaults alone may not suggest municipal insolvency. For example, a revenue bond, a type of special obligation bond, is payable "from the income of utilities or projects erected or constructed with the proceeds of the bond issue."[244] Therefore, because the revenue bond holder has no claim on municipal tax revenue,[245] the default on these special obligation bonds would not bind a city's general revenues and would not impact a city's ability to pay any other debts as they become due. Such bonds can be contrasted with general obligation bonds that are "payable from and secured by a pledge of the issuers taxing power."[246] The default of general obligation bonds would most likely indicate insolvency, unless, as in

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238 McConnell & Picker, *supra* note 54, 456.

239 11 U.S.C. § 101(32)(c).

240 *See In re* City of Bridgeport, 129 B.R. 332, 337 (Bankr. D. Conn. 1991) ("Section 101(32)(C)(ii) defines insolvency by whether Bridgeport will be able to 'pay its debts as they become due,' not on whether it has a budget gap.").

241 *See, e.g.*, *In re* Pierce Cnty. Hous. Auth., 414 B.R. 702, 710–11 (Bankr. W.D. Wash. 2009) (determining that the test for insolvency is a cash flow rather than a budget deficit analysis); *see also* Int'l Ass'n of Firefighters v. City of Vallejo (*In re* City of Vallejo), 408 B.R. 280, 288 (B.A.P. 9th Cir. 2009) (noting the trial court's finding that the city's reserves, operational deficit, and cash flow was sufficient to show insolvency).

242 *See, e.g.*, *In re* Ellicott Sch. Bldg. Auth., 150 B.R. 261, 265 (Bankr. D. Colo. 1992) (stating that the debtor was not insolvent because it had the ability to draw down from a reserve fund); *see also In re City of Vallejo*, 408 B.R. at 288 (noting that, because the reserve fund was depleted, the finding of insolvency was bolstered).

243 *In re City of Bridgeport*, 129 B.R. at 337.

244 15 MCQUILLIN, *supra* note 188, § 43.14 (citing Steele v. Indus. Dev. Bd., 301 F.3d 401 (6th Cir. 2002)).

245 *Id.* (citing *Steele*, 301 F.3d at 401).

246 64 AM. JUR. 2D *Public Securities and Obligations* § 13, at 39 (2001).

Bridgeport, there were available reserves from which the general obligation bond payments could be made.[247]

Under the above analysis, it would likely not be sufficient for a municipality merely to have an underfunded or even insolvent pension fund. Rather, the municipality would need to be either (a) not paying their pensions or other debts, as was the case of Prichard, Alabama[248] or, more likely, given the potential political backlash from such an action, (b) unable to pay their pension or other bond or operating obligations in either that fiscal year or in the next year, based on an adopted budget.[249]

2. Bankruptcy Court Power

Chapter 9 prevents a bankruptcy court from directing a municipality on how to spend its assets.[250] One bankruptcy court has interpreted this restriction as limiting the court's involvement in the bankruptcy plan and actions that would, in effect, "determine the municipality's future tax and spending decisions."[251]

While chapter 9 restricts the court from *directly* mandating how the municipality should spend assets,[252] the Code's definition of municipal insolvency might prompt municipalities to spend their resources or to direct property in a certain manner so as to be eligible to file under chapter 9. For example, to determine if the municipality was able to pay its debts, the court would look for a "tangible reserve fund from which debts could be paid."[253] Practically speaking, if a municipality were entering bankruptcy to address

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[247] *See In re City of Bridgeport*, 129 B.R. at 337 (citing 11 U.S.C. § 101(32)(c)); *see, e.g.*, *Ellicott*, 150 B.R. at 265 (stating that the debtor was not insolvent because it had the ability to draw down from a reserve fund); *see also In re City of Vallejo*, 408 B.R. at 288 (noting that, because the reserve fund was depleted, the finding of insolvency was bolstered).

[248] Cary Chow & Mike Jernigan, *Hearing Set for Prichard Pension Checks*, FOX10TV.COM (Mar. 4, 2010, 10:33 PM), http://www.fox10tv.com/dpp/news/Hearing-set-for-Prichard-pension-checks.

[249] *See In re City of Bridgeport*, 129 B.R. at 338.

[250] 11 U.S.C. § 904 (2006) ("Notwithstanding any power of the court, unless the debtor consents or the plan so provides, the court may not, by any stay, order, or decree, in the case or otherwise, interfere with (1) any of the political or governmental powers of the debtor; (2) any of the property or revenues of the debtor; or (3) the debtor's use or enjoyment of any income-producing property.").

[251] *See In re* Pierce Cnty. Hous. Auth., 414 B.R. 702, 715 (Bankr. W.D. Wash. 2009).

[252] 11 U.S.C. § 904.

[253] *In re Pierce Cnty.*, 414 B.R. at 712; *see also* Int'l Ass'n of Firefighters v. City of Vallejo (*In re* City of Vallejo), 408 B.R. 280, 288 (B.A.P. 9th Cir. 2009) (explaining that the depletion of the reserve fund bolstered the finding of insolvency); *In re* Ellicott Sch. Bldg. Auth., 150 B.R. 261, 265 (Bankr. D. Colo. 1992) (finding that debtor was not insolvent because it had the ability to draw down from a reserve fund).

pension obligations, a municipality would have to draw down on pension trust fund assets to pay current pension obligations, as the trust instrument allowed, and would have to pay current pension obligations out of general funds if pension assets were insufficient. Only if these efforts were insufficient to pay current pension obligations would a court be likely to declare a municipality "insolvent" under chapter 9.[254]

The most obvious initial impact in a chapter 9 proceeding to both the pensioner, as a creditor, and the municipality, as a debtor, would likely be the automatic stay.[255] A stay, in the case of a pension obligation, would pause almost any litigation[256] that the pensioners would pursue on the basis of state law.[257] There are a number of statutory exceptions to the stay. However, few if any of these would be applicable to an action to enforce a pension.[258] This leaves pensioners with no legal recourse throughout the progression of the bankruptcy other than through the bankruptcy court itself.[259]

3. *Federal Preemption*

Longstanding federal pre-emption doctrine has held that state law that conflicts with federal law is preempted.[260] The District Court for the Eastern District of California recently enforced this holding in *In re City of Vallejo* within the context of Tenth Amendment concerns of municipal bankruptcy.[261] This ruling has a number of potential impacts in a municipal pension debt scenario.

The court in *Vallejo* held that the city did not need to follow state law when rejecting collective bargaining agreements as executory contracts in chapter 9 bankruptcy proceedings.[262] In *Vallejo*, a city in California filed for bankruptcy and then unilaterally modified the terms of four collective bargaining

254 *In re City of Bridgeport*, 129 B.R. at 337; *see also In re Ellicott*, 150 B.R. at 265 (finding that debtor was not insolvent because it had the ability to draw down from a reserve fund).

255 *See* 11 U.S.C. §§ 362, 901.

256 *See* 3 COLLIER, *supra* note 87, at 362–25.

257 Ferrara, *supra* note 5.

258 11 U.S.C. § 362 (exceptions to the stay include family law matters, criminal law actions and tax actions, among others).

259 Certainly the political pressures inherent in cutting off a large number of citizens' income would make most cities shy away from this tool.

260 Int'l Bhd. of Elec. Workers v. City of Vallejo (*In re* City of Vallejo, CA), 432 B.R. 262, 269 (Bankr. E.D. Cal. 2010).

261 *Id.*

262 *Id.* at 270.

agreements.[263] The City of Vallejo then sought to have these rejected under the Code.[264] Several unions failed to reach an agreement with the city and subsequently challenged the rejection of these contracts, arguing that the city should have followed applicable California labor laws.[265]

While some commentators had previously thought that state law would trump bankruptcy law in the collective bargaining context, given chapter 9's deference to states,[266] the court in *Vallejo* sided with the city, reasoning that the state statute authorizing municipal bankruptcy did not in any way limit the rejection of employee contracts as a precondition[267] to seeking federal relief.[268] The court affirmed its previous holding in *In re County of Orange*, stating that "[a] state's authorization that its municipalities may seek chapter 9 relief is a declaration of state policy that the benefits of chapter 9 take precedence over control of its municipalities."[269]

The court noted that the procedure for rejection of a collective bargaining agreement was not incorporated into chapter 9.[270] Therefore, the Supreme Court's *Bildisco* standard should be followed for rejection of a collective bargaining agreement in municipal bankruptcy.[271] Collective bargaining agreements then, under municipal bankruptcy, are not subject to either state labor law or the § 1113 protections.

While some commentators[272] and local officials[273] have argued that state law restrictions on pension reduction or modifications may limit the

263 *Id.* at 265 (discussing the fact that the City of Vallejo sought to reject contracts under § 365).
264 *Id.*
265 *Id*. at 265–66.
266 McConnell & Picker, *supra* note 54, at 468.
267 Note that the court uses the term "pre-condition" and not "exception" to chapter 9, presumably because under *In re County of Orange* the court held, "By authorizing the use of [c]hapter 9 by its municipalities, California must accept [c]hapter 9 in its totality; it cannot cherry pick what it likes while disregarding the rest." Cnty. of Orange v. Merrill Lynch & Co. (*In re* Cnty. of Orange), 191 B.R. 1005, 1021 (Bankr. C.D. Cal. 1996).
268 *In re City of Vallejo*, 432 B.R. at 270.
269 *Id.* at 269 (citing *In re Cnty. of Orange*, 191 B.R. at 1021).
270 *Id.* at 267 (citing § 901 and noting that, because this section did not incorporate § 1113, the collective bargaining provision did not apply).
271 *Id.* at 272.
272 Girard Miller, *Benefits, Bankruptcy and Baloney*, GOVERNING MAGAZINE, July 8, 2010, *available at* http://www.governing.com/columns/public-money/state-retiree-Benefits-Bankruptcy-and-Baloney.html (arguing that cities with provisions restricting the alteration of pension benefits in statute would have an easier time modifying these benefits in bankruptcy than would cities in states where benefits were protected in the state's constitution).

bankruptcy court's ability to reduce or terminate these retirement obligations, the court in *Vallejo* affirmed the general proposition that, where states authorize a municipality to file bankruptcy, federal bankruptcy law is not subordinate to state law.[274] Although the California Code authorized cities to invoke municipal bankruptcy,[275] other provisions conflicted with municipal bankruptcy law.[276]

4. Collective Bargaining Agreements and Executory Contracts

How a retiree's claim for a pension is treated in bankruptcy depends, in large part, on the court's interpretation of the Code, as well as the origin of the grant of the employee pension (i.e., whether they were given a pension under a collective bargaining agreement or employment contract). In the case of a pension benefit included in the terms of a collective bargaining agreement, the obligation could be rejected with the bankruptcy court's approval utilizing the Supreme Court's *Bildisco* standards.[277] After such a rejection, the public pensioners would then become creditors with claims of damages for the discharged contract obligations.[278]

Whether the pensions for those retirees who have vested benefits or who are already retired would be eligible for rejection hinges on the definition of "executory."[279] Congress avoided any attempt to adopt a concrete definition for the term executory.[280] The courts have utilized different approaches in defining "executory."[281] As mentioned above, many courts have adopted the

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273 Jan Goldsmith, *San Diego Bankruptcy Talk is Nonsense*, SIGN ON SAN DIEGO (Nov. 14, 2010, 12:00 AM), http://www.signonsandiego.com/news/2010/nov/14/san-diego-bankruptcy-talk-nonsense/.

274 *In re City of Vallejo*, 432 B.R. at 270 ("[T]he city is permitted to reject the IBEW CBA as part of its [c]hapter 9 bankruptcy reorganization without limitation by state labor law.").

275 *Id.* at 268 (citing CAL. GOV'T CODE § 53760 (West 2011)).

276 *Id.* at 271 (citing CAL. GOV'T CODE § 3500 (West 2011)).

277 *Id.* at 272.

278 11 U.S.C. § 365(o) (2006); *see, e.g.*, Order Approving Stipulation and for Rejection of Collective Bargaining Agreement, *In re* City of Vallejo, 403 B.R. 72 (Bankr. E.D. Cal. 2009) (No. 2008-26813).

279 11 U.S.C. § 365.

280 Heiman, *supra* note 107, at 228.

281 *See, e.g.*, *In re* Surfside Resort & Suites, 344 B.R. 179, 186 (Bankr. M.D. Fla. 2006) (determining whether a contract is executory is based on "benefits that assumption or rejection would produce for the estate"); *see also* Sharon Steel Corp. v. Nat'l Fuel Gas Distrib. Corp., 872 F.2d 36, 39 (3d Cir. 1989) (noting that prior courts looked to legislative history to define an executory contract as a "contract on which performance remains due on both sides" (citing NLRB v. Bildisco & Bildisco, 465 U.S. 513, 526 (1984), *partially superseded by statute*, Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, 98 Stat. 376)).

Countryman definition, requiring that both parties have outstanding obligations under the contract to consider a contract "executory."[282]

A minority of courts,[283] however, have adopted a functional definition of executory contracts, looking to the purposes for which § 365 (dealing with the assumption and rejection of executory contracts) was passed and even approving rejections in cases in which one side argued completion of its duties under the contract.[284] Typically, something in addition to payment by one party must be due by the terms of the contract to consider a contract executory. Otherwise, the party owed money under the contract is merely a creditor and is treated accordingly.[285] There may be an argument that a pension agreement between a pensioner and a municipality is an executory contract if pension benefits are conditioned on an employee avoiding certain behavior, and thus, benefits are subject to divestment.[286] For example, a municipal pension may provide for divestment if a pensioner is convicted on criminal charges.[287]

Pension benefits included as part of an employment or other type of contract would likely not be considered "executory" for retired or vested[288] pensioners since the action owed by the pensioner—employment in the service of the municipality—is completed and all that is owed by the government is payment of the pension.[289] In a case involving pension obligations owed to retired or vested pensioners, the bankruptcy court would most likely not allow the municipality to reject these pension agreements as executory contracts.

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282 Heiman, *supra* note 107, at 228.

283 Ellman & Merrett, *supra* note 194, at 392–93.

284 *See, e.g.*, *In re Surfside Resort & Suites*, 344 B.R. at 186 (determining "whether a contract is executory is based on 'benefits that assumption or rejection would produce for the estate'" (quoting Sipes v. Atl. Gulf Cmtys. Corp. (*In re* Gen. Dev. Corp.), 84 F.3d 1364, 1375 (11th Cir. 1996))).

285 *See Bildisco*, 465 U.S. at 522 n.6 (defining the term executory contract as one "'on which performance is due to some extent on both sides'" (quoting H.R. REP. NO. 95-595, at 347 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6303)); *see also In re* Norquist, 43 B.R. 224, 228 (Bankr. E.D. Wash. 1984).

286 *But see In re* Teligent, Inc. 268 B.R. 723, 729 (Bankr. S.D.N.Y. 2001) (finding that the contract was executory even though it contained a non-compete clause).

287 *See, e.g.*, 43 PA. STAT. ANN. §§ 1311–1315 (West 2011) (denying pension benefits to public employees and elected officials who plead guilty or are convicted of certain crimes).

288 *See* Mascio v. Pub. Emps. Retirement Sys. of Ohio, 160 F.3d 310, 313 (6th Cir. 1998) (explaining that the term "vested" means that the pensioner has fulfilled conditions that give the pensioner a right to the pension that "cannot afterwards be impaired or revoked"). This can be contrasted with a retired employee, for example, because a retirement system might require ten years of service for the employee to "vest" in the system but only give benefits upon the employee's reaching the age of sixty. An employee after ten years of service is said to "vest" in the retirement system even though they might continue to work for the employer or leave to work for another. *See, e.g.*, GA. CODE ANN., § 47-3-129(a) (West 2011).

289 *See Executory Labor Contracts and Municipal Bankruptcy*, 85 YALE L.J. 957, 964–65 n.43 (1976).

Instead, the court would likely view pension obligations as any other current financial obligation, and pensioners would be analogous to creditors with a claim for the value of the unfunded pension obligations.[290] Even if the court allowed the municipality to reject a pension obligation as an executory contract, the pensioners would have a claim for damages against the municipality as creditors[291] and, therefore, would enjoy the same rights, and the municipality would be subject to the same obligations, regardless of how the court classified the obligation.

5. Claim Amount

Assuming that the bankruptcy court allowed municipal retirees, pension funds, or other relevant creditors to make claims for municipal pension obligations, the court would then need to determine the amount of the claims.[292] Determining the claim value for unpaid, past-due pension obligations would be more certain, but the bankruptcy court would most likely need to rely upon actuarial tables[293] to determine the claim value for future pension obligations[294] and would discount the claim amount to reflect its present value.[295] In chapter 11 cases, the PBGC, as the ultimate insurer of municipal pensions, brings both valuation expertise and advocacy experience concerning the valuation of pension claims.[296] A single pensioner acting as a creditor or a group of pensioners acting as creditors would not have the requisite level of expertise. Therefore, in a chapter 9 proceeding, determining a fair value for the pension claim could place a great burden on a bankruptcy court exercising its authority.[297]

One of the major protections for pensions in chapter 11 is found in ERISA.[298] An ERISA provision requiring that the court declare pension termination "necessary for reorganization"[299] can be compared with the "best

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290 *See, e.g.*, 11 U.S.C. §§ 922, 943 (2006).
291 *Id.* § 502(g).
292 *Id.* §§ 502(b), 901.
293 *See, e.g.*, Pletz v. United States (*In re* Pletz), 221 F.3d 1114, 1116 (9th Cir. 2000) (consulting actuarial tables to determine the value of property owned by tenants by the entirety).
294 11 U.S.C. § 502(b).
295 3 NORTON, *supra* note 52, § 48.11, at 48–27.
296 *See, e.g.*, CSC Indus., Inc. v. Belfance (*In re* CSC Indus., Inc.), 232 F.3d 505, 507–08 (6th Cir. 2000) (PBGC argued in a bankruptcy proceeding about the value of unfunded benefit liability claims in a pension plan); *see also In re* U.S. Airways Grp., Inc., 303 B.R. 784, 792 (Bankr. E.D. Va. 2003).
297 11 U.S.C. § 502.
298 29 U.S.C. § 1341.
299 *Id.* § 1341(c)(2)(B)(ii)(IV).

interest of the creditors" test under chapter 9,[300] in which a plan is confirmed if the plan is "all a creditor can reasonably expect."[301] The "necessary for reorganization" test ERISA provides recognizes that a pensioner holds a unique debt obligation and considers whether retaining the pension would "hold up" other creditors from invoking a reorganization plan, by requiring the court to determine that "unless the plan is terminated, such person will be unable to pay all its debts pursuant to a plan of reorganization and will be unable to continue in business outside the chapter 11 reorganization process."[302] The "best interest of the creditors" test, on the other hand, considers the specific proposed plan of chapter 9 reorganization, groups pensioners with other municipal creditors, and asks whether the plan that the municipality proposes gives creditors what they would expect given the constraints of municipal revenue.[303]

C. Gaps in Federal Municipal Bankruptcy Law

Chapter 9 lacks some of the procedural and administrative processes intended to provide protection for pensioners in chapter 11 bankruptcy procedures.[304] The lack of these protections creates significant gaps in federal municipal bankruptcy statutes.

While Congress contemplated including § 1113 protections in chapter 9,[305] the *Vallejo* decision highlights that chapter 11 has necessary procedural and substantive preconditions for rejecting collective bargaining agreements[306] that are not included in chapter 9.[307] Some have posited that § 1113 may have been omitted from chapter 9 in deference to state law[308] and pension protection already provided at the state level. However, the short period in which

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300 Vasquez & Daucher, *supra* note 119, at 51.

301 5 NORTON, *supra* note 52, § 90.20, at 90-45.

302 11 U.S.C. § 1341(c)(2)(B)(ii)(IV).

303 *See* 5 NORTON, *supra* note 52, § 90.20, at 90-46.

304 *See*, *e.g.*, 11 U.S.C. § 1113; 29 U.S.C. § 1341(a).

305 Orange Cnty. Emps. Ass'n v. Cnty. of Orange (*In re* Cnty. of Orange), 179 B.R. 177, 183 n.15 (Bankr. C.D. Cal. 1995); Int'l Bhd. of Elec. Workers Local 2376 v. City of Vallejo (*In re* City of Vallejo), 432 B.R. 262, 271 (Bankr. E.D. Cal. 2010) ("The legislative history of the Bankruptcy Reform Act of 1994 ("1994 Act"), Pub. L. No. 103-394, 103d Cong, 2d Sess., 108 Stat. 4106, indicates that Congress contemplated enacting a '§ 1113-like' statute for [c]hapter 9.").

306 *See* 11 U.S.C. § 1113.

307 *See id.* §§ 901, 1113.

308 *In re City of Vallejo*, 432 B.R. at 271 ("The Court reasoned that Congress may have decided against adding a [§] 1113 to [c]hapter 9 out of concern about encroaching on states rights under the Tenth Amendment."). Note, of course, that under *Vallejo*, no such deference is given. *Id.* at 268.

Congress passed § 1113 after the Supreme Court's decision in *Bildisco* is more insightful.[309] The arguably modest impact of § 1113 on employees,[310] the rarity of municipal bankruptcy filings,[311] and the fact that *Vallejo* was a district court opinion may also account for Congress's inaction in comparison to its swift action following *Bildisco*.[312]

Congress provided significant protection for pensions in § 1113 by requiring a court to review applications to reject collective bargaining agreements in an expedited time period.[313] This expedited time frame would be significant should a municipality seek to reorganize or terminate pension obligations. As the case of Prichard, Alabama highlights, having a court review a municipality's underlying claims in bankruptcy in an expedited manner would ensure that pensioners are not crushed under the "hammer" of the bankruptcy stay longer than is necessary.

Additionally, the Code provisions requiring payment and giving a claim in the case of bankruptcy for a multi-employer plan provide protections for the other parties in a joint pension trust.[314] Contrast this with the status of a multi-employer government trust that is held hostage to potential spillover effects[315] if a single employer terminates pensions in a multi-employer municipal fund. This could result in increased premium costs for the remaining employers. While this impact might be negligible for a small municipality in a multi-employer fund, the impact could be significant in a large-scale municipal bankruptcy.

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[309] *See* Century Brass Prods., Inc. v. UAW Local 1604 (*In re* Century Brass Prods., Inc.), 795 F.2d 265, 273 (2d Cir. 1986) (noting that § 1113 was passed within five months of *Bildisco* and therefore had relatively little legislative history); *see also* McConnell & Picker, *supra* note 54, at 467–68 (positing that the absence of § 1113 was due either to inadvertence or a belief that "given the special deference paid to state law in chapter 9 through § 903, state law might be understood to override the power to reject under § 365").

[310] *See* Dawson, *supra* note 170, at 118–19 ("[T]he fact that every large corporate debtor during a seven year period was able to reject its [collective bargaining agreement] suggests that the statute has provided very little protection at all."). *But see id.* at 113 (noting that a study of the first nine years after § 1113 was implemented, the rejection rate for collective bargaining agreements dropped from 67% to 58%).

[311] *See* McGrath & Kim *supra* note 20, at 14 ("There have only been approximately 566 [c]hapter 9 filings.").

[312] *See* Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, § 541(a), 98 Stat. 376, 390; *In re Century Brass Prods.*, 795 F.2d at 273 (noting that Congress quickly responded to the Supreme Court's ruling in *Bildisco* by passing § 1113 five months later).

[313] 11 U.S.C. § 1113 (d)(1)–(2) (2006).

[314] 29 U.S.C. § 1341(a).

[315] Tung, *supra* note 84, at 905–06 (using the phrase "spillover effects" to describe the impact of municipal bankruptcy on the borrowing costs for municipalities neighboring a city invoking chapter 9).

However, PBGC pension guarantees, the primary protection for municipal pensioners, would not be applicable in a chapter 9 proceeding. While there are limitations to PBGC benefits,[316] an estimated 85% of employees who received benefits through the PBGC after their pension plans were terminated received full benefits.[317] There is no "Public Pension Guarantee Corporation" acting as an "insurance policy" for terminated public pensions; thus, pensioners would likely receive only a small fraction of their pensions or less as creditors in a municipal bankruptcy proceeding.

While Congress has not added specific protections for pensioners in chapter 9, the strong language in the committee reports associated with § 1114, which protects retiree benefits,[318] and the swift action in passing § 1113[319] suggests that Congress historically favored protecting the rights of retirees. For political reasons, changes to chapter 9 and state law likely would be necessary to enable a municipality to use chapter 9 to manage public pension obligations. Admittedly, any "solution" to the public pension problem is imperfect, but changes are needed at both the state and federal levels to enable cities to deal with pension insolvency more effectively from both a preventative and, more importantly given the current state of the economy, a distressed debtor perspective.

V. Proposed Changes to Protect Pensioners and Local Governments

A. Preventative Measures: A Day Late and [Billions of Dollars] Short

Preventative measures, the easiest method available for municipalities to address pension shortfalls or prospective changes in future retirement benefits,[320] are unable to provide a municipality short-term relief. Nonetheless, systematic and long-term changes to municipal retirement benefit programs are necessary to provide lasting stability for both municipalities and pensioners.

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316 29 U.S.C. § 1322(b).

317 Keating, *supra* note 128, at 807.

318 134 CONG. REC. 12,697 (1988).

319 Century Brass Prods., Inc. v. UAW Local 1604 (*In re* Century Brass Prods., Inc.), 795 F.2d 265, 273 (2nd Cir. 1986); *see also* McConnell & Picker, *supra* note 54, at 467.

320 Prospective changes are easiest because they will not violate state statute or constitutional limits on changes to pension benefits. *Pensions*, *supra* note 196, § 1176.

While some municipalities have reduced pension plan benefits and increased the retirement age at which benefits are paid to new employees,[321] municipalities should also implement a more sustainable model by migrating to a defined contribution plan, more commonly known as a 401(k) plan,[322] for future employees.[323] Shifting to defined contribution plans would allow a municipality to closely associate contribution obligations to benefits provided because these plans only require municipal contributions during the time the employee is serving the municipality.[324] This also prevents future employees and taxpayers from having to pay a disproportionate share of costs that do not directly benefit them. Additionally, such a change would help a pensioner in a bankruptcy scenario because bargaining power of current employees likely would be far greater than that of retirees since retiree contributions are necessary to provide current municipal services.

States should also consider explicitly adding municipal pension obligations to existing constitutional limitations on municipal debt. Many state constitutions include municipal debt limits[325] restricting the assumption of debt beyond a certain amount[326] or requiring voter approval for municipalities to assume debt exceeding revenue within a given fiscal year.[327] These limits came about in part because of a belief that "the benefits of debt creation tend to be

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[321] *See, e.g.*, Sarah Coppola, *Austin City Council OKs Pension Plan Changes*, STATESMAN.COM (Oct. 14, 2010, 11:03 AM), http://www.statesman.com/blogs/content/sharedgen/blogs/austin/cityhall/entries/2010/10/14/austin_city_council_oks_pensio.html.

[322] 26 U.S.C. § 457 (2006) (mandating that governmental 401(k) plans that were in existence as of May 1986 were grandfathered in when the 1986 Tax Reform Act was passed; however, government entities as a general rule are unable to offer 401(k) plans). Government entities may offer defined contribution plans. *See* Paul M Secunda, *Constitutional Contracts Clause Challenges in Public Pension Litigation*, 28 HOFSTRA LAB. & EMP. L.J. 263, n.25 (2011) (noting that "43% of state workers and 24% of local workers had access to defined contribution plans" (citing *State and Local Government Employee Benefits, March 2010*, U.S. BUREAU OF LABOR STATISTICS (Mar. 9, 2011), http://www.bls.gov/opub/ted/2011/ted_20110309.htm)).

[323] SNELL, *supra* note 209, at 3 (finding that only four states (Alaska, Michigan, Nebraska, and West Virginia) and the District of Columbia have shifted to mandatory defined contribution plans for new employees).

[324] This solution, of course, would not address the impacts of future retiree healthcare costs. Again, since many states allow public employers to change these benefits at any point, these obligations are less problematic from a pure "debt perspective." *See, e.g.*, Doyle v. City of Medford, 606 F.3d 667, 669 (9th Cir. 2010). However retiree healthcare costs continue to provide issues from a political perspective. This problem deserves further review.

[325] *See* Stewart E. Sterk & Elizabeth Goldman, *Controlling Legislative Shortsightedness: The Effectiveness of Constitutional Debt Limitations*, 1991 WIS. L. REV. 1301, 1313 n.72 (1991) (citing HAW. CONST. art. VII, § 3; IND. CONST. art. XIII, § 1; N.Y. CONST. art VIII, § 4).

[326] GA. CONST. art. IX, § 5, ¶ I (limiting local government debt to "10 percent of the assessed value of all taxable property" and requiring voter approval for taking on local government debt).

[327] *See, e.g.*, CAL. CONST. art. XVI, § 18.

concentrated in well-organized groups while its costs tend to be dispersed throughout the population."[328] If a municipality was required to seek voter approval when creating new pension obligations, the voting process likely would serve as a check on short-sighted assumptions of pension obligations that future taxpayers would ultimately fund. Additionally, including pension obligations in a total debt cap is logical given their long-term nature and is consistent with general policies supporting debt limits and "[controlling] excess borrowing by municipalities."[329]

B. Curative Measures: Changes to Federal Municipal Bankruptcy

A former bankruptcy judge described municipal bankruptcy as "[t]he best of a bad deal. The best that everybody can see making out of a mess."[330] Indeed, a municipality that invokes chapter 9 must contend with the same challenges as any other debtor. Additionally, there are immediate consequences for neighboring local governments, an effect unique to chapter 9 bankruptcies.[331] However, chapter 9 is one of the only available tools for managing pension obligations when a municipality is insolvent; therefore, it is worth examining how this tool might be refined to further its purpose[332] in the face of growing municipal pension burdens.[333]

Congress has repeatedly taken a reactionary approach when amending the Code and other federal laws to accommodate the rights of the individual worker.[334] While one might argue that these amendments represent a continual erosion of treating "like creditors alike,"[335] individual workers affected by a municipality's inability to honor pension obligations exert strong political

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328 Sterk & Goldman, *supra* note 325, at 1365.

329 Fred L. Morrison, *The Insolvency of Public Entities in the United States*, 50 AM. J. COMP. L. 567, 569 (2002).

330 Adam Levitin, *Experts Examine Municipal Financial Distress*, AM. BANKR. INST. J., Dec. 2009–Jan. 2010, at 28, 79.

331 Tung, *supra* note 84, at 904 (noting that after Orange County went into bankruptcy, other local governments within the state were required to offer an estimated fifteen to twenty-five higher basis points on short term notes).

332 *In re* City of Bridgeport, 129 B.R. 332, 336–37 (Bankr. D. Conn. 1991) (citing H.R. REP. NO. 100-1011, at 2 (1988), *reprinted in* 1988 U.S.C.C.A.N. 4115, 4116).

333 Cnty. of Orange v. Merrill Lynch & Co. (*In re* Cnty. of Orange), 241 B.R. 212, 214 (Bankr. C.D. Cal. 1999) ("In 1994, Orange County, California, filed the largest municipal bankruptcy in history after failure of a risky leveraged investment scheme by its Treasurer.").

334 *See, e.g.*, 11 U.S.C. §§ 1113–1114 (2006); 29 U.S.C. §§ 1001–1461.

335 *See In re* Nehring, 84 B.R. 571, 578 (Bankr. S.D. Iowa 1988) ("[T]he bankruptcy court undoubtedly will consider the strong policies of the Bankruptcy Code to treat like creditors alike and to grant the debtor a new start, and the equities of the events . . . ." (internal quotation marks omitted)).

pressure on both Congress when it amends federal laws and local governments when they decide how to manage increasing debt. Under the current political structure, it would be difficult for a municipality to reduce pension obligations even though such reductions are allowable through municipal bankruptcy proceedings.[336] chapter 9 lacks the employee-pensioner protections found in both chapter 11[337] and state laws.[338] These protections not only leave municipal employees and retirees vulnerable, but also leave municipalities hamstrung and arguably hesitant to use municipal bankruptcy as a tool to restructure pension obligations.

Chapter 9 should explicitly include protections for workers. Judges should review pension debts in an expedited fashion akin to those in § 1113,[339] ensuring that a Prichard, Alabama, scenario, where pensioners had to wait nearly six months to determine the status of pension debts, is not repeated. Additionally, the equitable principles for collective bargaining agreements set forth in *Bildisco*[340] and further articulated in § 1113[341] should be explicit in chapter 9. Finally, chapter 9 should include the ERISA "necessary to the plan" test as a threshold requirement to terminate a pension. These changes acknowledge the unique role a pensioner plays in bankruptcy proceedings.

Not every retiree protection present in chapter 11 is feasible in chapter 9. While the ERISA provision allowing PBGCs to assume under-funded, terminated pensions arguably provides the greatest protection for pensioners under chapter 11,[342] the establishment of a similar insurance program in chapter 9 may be difficult to implement. The current funding shortfalls in state and municipal pensions as well as distressed nature of state and local government budgets likely would result in unaffordable insurance premiums. Furthermore, political resistance to such a program likely would be extensive

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336 Steven Greenhut, *Vallejo's Painful Lessons in Municipal Bankruptcy*, WALL ST. J., Mar. 26, 2010, http://online.wsj.com/article/SB10001424052748703625304575115551578762006.html.

337 11 U.S.C. § 1113.

338 *See, e.g.*, Withers v. Register, 269 S.E.2d 431, 432 (Ga. 1980); *see* ALASKA CONST. art. XII, § 7; MICH. CONST. art. IX, § 24; *Pensions*, *supra* note 196, § 1176.

339 11 U.S.C. § 1113(d)(1)–(2).

340 NLRB v. Bildisco & Bildisco, 465 U.S. 513, 521 (1984) (noting that a court must consider whether the "equities balance in favor of rejection" to determine whether to reject a collective bargaining agreement), *partially superseded by statute*, Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, 98 Stat. 376.

341 11 U.S.C. § 1113(c)(3) (stating that the court must consider "the balance of the equities").

342 29 U.S.C. §§ 1322–1323.

given the budget shortfalls facing the PBGC today[343] and historical resistance to federal regulation of state and local government functions.[344]

C. Curative Measures: Changes to State Authorizing Statutes

In addition to these changes to the Code, states should consider establishing minimum requirements a municipality must meet before invoking chapter 9.[345] A state blindly allowing a municipality to file bankruptcy could not limit a municipality's ability to restructure pension obligations under the Code,[346] but a state requiring municipalities to appear before a pension review committee prior to filing bankruptcy may be able to monitor these changes. Such a committee could evaluate the solvency of a municipality's pension trust and make an initial determination of the municipality's ability to pay outstanding obligations. Members of a committee serving in this capacity should include financial experts who could bring the same level of analysis and expertise to public pensions that the PBGCs expert personnel bring to private pensions. This review process would provide an additional layer of protection for pensioners by providing initial assessments of the extent to which a municipality is insolvent as well as protection from the harsh consequences of the automatic stay.[347]

This prebankruptcy filing step recognizes pension obligations as a substantial component of municipal debt, and the process would encourage municipalities to include pension debt reorganization in any chapter 9 filing. This could ensure that municipal bankruptcy is a more effective long-term debt management tool. Additionally, this prebankruptcy review could provide a greater level of protection for municipalities within the state against the spillover effects of individual municipal bankruptcies.[348]

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343 Olivia S. Mitchell, *Retirement Risk Management in Times of Turmoil*, 17 ELDER L.J. 439, 453 (2010) ("Unfortunately, the PBGC itself faces shortfalls. In a very short time span, the system went from a surplus position (having close to $10 billion in the late 1990s) to a staggering deficit more recently.").

344 While I argue that applying PBGC coverage to government entities would be politically impossible, I concede that pension insurance would provide needed protections for local government pensioners and should be considered, perhaps in a more stable economic environment.

345 *See* Tung, *supra* note 84, at 887 (noting that some states already impose preconditions for a municipality to file for chapter 9 bankruptcy).

346 *See* Cnty. of Orange v. Merrill Lynch & Co. (*In re* Cnty. of Orange), 191 B.R. 1005, 1021 (Bankr. C.D. Cal. 1996) ("By authorizing the use of chapter 9 by its municipalities, California must accept chapter 9 in its totality.").

347 11 U.S.C. § 943.

348 Tung, *supra* note 84, at 905–06 (2002).

State authorization of municipal bankruptcy is the exception rather than the rule.[349] While a host of political and pragmatic considerations influence whether a state allows its municipalities to access the federal bankruptcy courts, economic reality at the municipal level coupled with financial pressures at the state level may force some states to reconsider this historically resistant stance. If states choose to authorize their municipalities to file bankruptcy, they should recognize chapter 9's potential as a method of successfully managing pension obligations and include safeguards for municipal employees, such as the proposed pension review process.

CONCLUSION

As the case of Prichard, Alabama highlights, using chapter 9 to address pension obligation problems result in a host of potential issues, not the least of which is political pressure from municipal retirees. The relationship of the "debtor" as elected official and the "creditor" (i.e., the pensioner) as voter creates a powerful disincentive for elected officials to reorganize their pension obligations in bankruptcy. Indeed, the maxim "an ounce of prevention is worth a pound of cure" carries particular weight here. Municipalities should make systemic, forward-looking changes to their retirement benefits. However, it is unlikely that preventative measures alone will be sufficient for many municipalities that are losing their ability to provide basic services because of looming pension obligations.

To make chapter 9 a politically feasible and financially pragmatic option, Congress should amend chapter 9 and provide protections given pensioners under other forms of bankruptcy. States should also perform internal reviews of municipal pension obligations as a prerequisite to filing for chapter 9. Encouraging states to authorize municipalities to file bankruptcy and adding provisions to protect pensioners in chapter 9 would help make "the best of a

349 ALLEGHENY INSTITUTE, *supra* note 15 (observing that currently, only nineteen states authorize municipal bankruptcy).

bad deal"[350] and could make the chapter 9 option politically feasible for municipalities with few other ways out.

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[350] Levitin, *supra* note 330, at 79.

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