

# Jim Spiotto

---



# **Municipal Finance Data Forum Midwest – Northern Illinois University**

## **Coming Attractions and Best Practices in Disclosure, Financial Distress and Related Data Standards for State and Local Governments**

### **What You Wished You Knew and Prepared for Before It Happened!**

James E. Spiotto  
Chapman Strategic Advisors L.L.C.  
312.845.3763  
[spiotto@chapmanstrategicadvisors.com](mailto:spiotto@chapmanstrategicadvisors.com)

October 3, 2019

© 2019 by James E. Spiotto. All rights reserved. James E. Spiotto is the Co-Publisher of Muninet Guide and a retired partner of Chapman and Cutler LLP as well as Managing Director of Chapman Strategic Advisors LLC and President of JASSEE Advisors, LLC. This document is for informational purposes, general in nature and based on authorities that are subject to change. It is not intended as a recommendation or advice, legal or otherwise, with regard to any action or inaction to be taken. The views expressed herein are solely those of the author and do not reflect the position, opinion or views of Chapman and Cutler LLP or Chapman Strategic Advisors LLC.

# Table of Contents

I.	The Gathering Storm of Economic Downturn and Increased Corporate Defaults That Can Cause Further State and Local Government Financial Distress	7
A.	What we have learned from the past about economic cycles	7
B.	Who will feel the adverse effects of the economic downturn?	18
II.	Need for Timely and Complete Continuing Disclosure on Material Events during Financial Distress of State and Local Government	19
A.	The panic of financial distress can be reduced or eliminated by full and prompt disclosure of the financial situation and the evolving situation	19
B.	Use of early warning signs	20
C.	Use of "better" financial reporting models	25
D.	Tell one tell all is the best practice	26
E.	Disclosure may be the workout or resolution's best friend	26
F.	Checklist of disclosures to maximize market acceptance in evaluating repayment of bond debt and to help bondholders and trustees in asserting their rights and interests	27

# Table of Contents

III.	Need to Educate the Municipal Market as to the Myth and Reality of Financial Distress of State and Local Governments Through Enhanced Disclosure	29
A.	Undisputable need for full, clear and accurate disclosure of the financial conditions and resolution alternatives of a distressed issuer	29
B.	The challenge of municipal disclosure	30
C.	Education of and disclosure to the market and investors is essential	32
IV.	The Historic Risk of Financial Distress and Bankruptcy of Issuers in the Municipal Market	33
A.	Historical default rate	33
B.	Recent default rate	37
C.	U.S. municipal defaults and recovery 1970-2013	40
D.	Defaults 2012-2017	42
E.	Bankruptcy	43
F.	Causes of bankruptcy	45
G.	Current use of Chapter 9	47
H.	Defaulted municipal bond recovery rates	59

# Table of Contents

V.	Whether the Municipality Can File for Chapter 9 Bankruptcy?	66
A.	No Chapter 9 for states	66
B.	Who can be a Chapter 9 debtor?	66
C.	Ability to be paid if the issuer is not authorized to file Chapter 9	70
VI.	What Is the Source of Payment?	71
A.	Determining the type of obligation and the source of payment	71
B.	Summary of types of bonds and treatment in Chapter 9	72
C.	Summary of Chapter 9 priorities	76
VII.	Is There a Lack of Diversification of Tax Sources and Limits on Taxes That Could Realistically Be Triggered	82
A.	Diversification of tax sources to prevent over-concentration of source of funding	82
B.	The need to reexamine the future viability of current tax revenue sources and consider new policies and sources for taxes to survive the digital, shared economy and artificial intelligence revolution	90

# Table of Contents

---

VIII. Is Effective State Oversight and Assistance Available to Prevent Defaults or Aid a Financially Troubled Municipality?	94
A. Growing and increased use of state oversight, supervision and assistance for emergencies of local governments	94
B. States recognize the use of a municipal receiver	100
C. Financial control boards and active supervision examples	101
D. Development of a Municipal Protection Commission as a quasi judicial entity to determine what costs are sustainable and affordable and which are not, including labor costs and benefits and whether taxes should be raised or costs reduced	102
E. The structure for oversight and emergency financing	102
F. Applicable state assistance, refinancing and restructuring mechanism should be disclosed	105

# Table of Contents

---

IX.	The Need for Uniform Pension Underfunding Disclosure and Whether Such Underfunding Is Crowding Out Funding of Essential Services and Needed Infrastructure	106
A.	State and local government pension funds status	106
B.	Many state and local governments have no current pension fund problem or have resolved it	109
C.	The aging population and possible future economic downturn are reasons to be vigilant no matter the current conditions of the pension fund	110
D.	Recent pension reform and litigation	111
E.	Examples of recent pension reforms and pension reform litigation	112
F.	What can be adjusted as to pension benefits	117
G.	Benefits of a uniform disclosure of pension funding and underfunding	118
H.	Funding of underfunded pension obligations should not impair or limit full funding of essential services and needed infrastructure	119
I.	The need to reinvest in state and local governments	122

# Table of Contents

---

APPENDIX I – General Overview of a 50 State Survey of Rights and Remedies Provided by States to Investors Relating to Government Bond Debt and State Oversight and Supervision of Financial Emergencies and Authorization to File Chapter 9 Bankruptcy	125
---	-----



# I. The Gathering Storm of Economic Downturn and Increased Corporate Defaults That Can Cause Further State and Local Government Financial Distress

---

## A. What we have learned from the past about economic cycles:

1. Recent recessions. There have been 11 economic recessions since 1948, namely, November 1948-October 1949 (11 months); July 1953-May 1954 (10 months); August 1957-April 1958 (8 months); April 1960-February 1961 (10 months); December 1969-November 1970 (11 months); November 1973-March 1975 (16 months); January 1980-July 1980 (6 months); July 1981-November 1982 (16 months); July 1990-March 1991 (8 months); March 2001-November 2001 (8 months); and the Great Recession of December 2007-June 2009 (18 months).
2. Time periods between recessions. In the recent past, recessions (economic downturns) have lasted from 6 to 18 months and have occurred, prior to 2008, every 1 to 9 years. It has been over 10 years since the end of the Great Recession. An economic downturn is past due.

# I. The Gathering Storm of Economic Downturn and Increased Corporate Defaults That Can Cause Further State and Local Government Financial Distress

## 3. Past indicators of an economic downturn:

### (a) Inverted yield curve:

- When short-term rates for government bonds are higher than the long-term rates, there is an inverted yield curve. On August 14, 2019, the yield on 2-year treasuries rose above the 10-year treasury yield. This happened before the 2001 recession on January 31, 2000 and before the 2007 recession on July 17, 2006. The inverted yield curve happened 14 months and 16 months, respectively, before the 2001 and 2007 recessions.

### (b) Peak in mergers and acquisitions:

- In the past, the peak in mergers and acquisitions and issuance of high yield debt has been followed by a dramatic rise in the default rate for corporate debt obligations in the next three years.
- This is corporate debt indigestion.

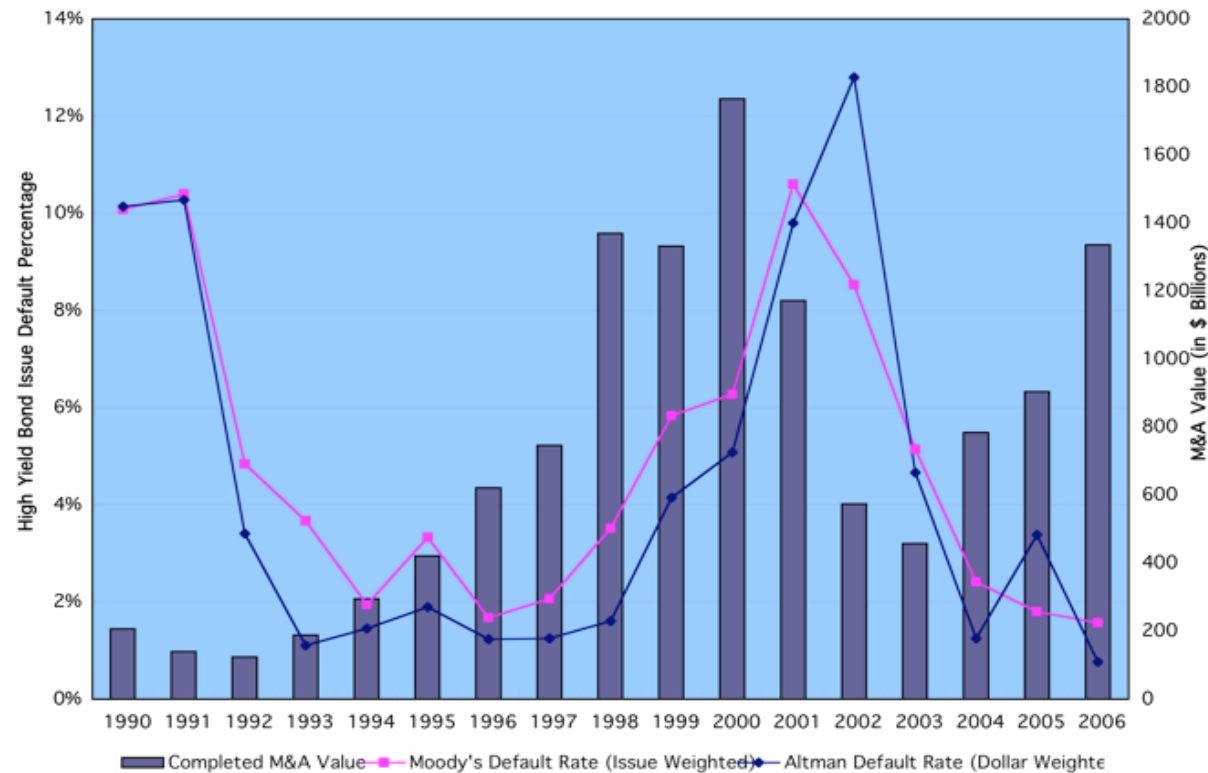
# **I. The Gathering Storm of Economic Downturn and Increased Corporate Defaults That Can Cause Further State and Local Government Financial Distress**

---

- In June 2007, announced global mergers and acquisitions for the first half of 2007 hit an all time high of \$2.8 trillion, up from \$1.9 trillion announced for the first half of 2006. Most of these did not actually close.
- Likewise, there was a peak in mergers and acquisitions in 2000 of about \$1.8 trillion. The peak in mergers and acquisitions both in 2000 and 2007 was followed by record peaks within 2 years of corporate defaults.
- Can it happen again? YES.
- In 2009, there were 9,466 mergers and acquisition in the USA for a value of \$877.6 billion and, by 2018, there were 14,883 mergers and acquisitions for a value of \$1.903 trillion. The value of mergers and acquisitions in less than 10 years more than doubled and reached the high in 2000.
- Will corporate debt indigestion follow? Will it cause loss of taxable income and sales that results in less tax revenue?

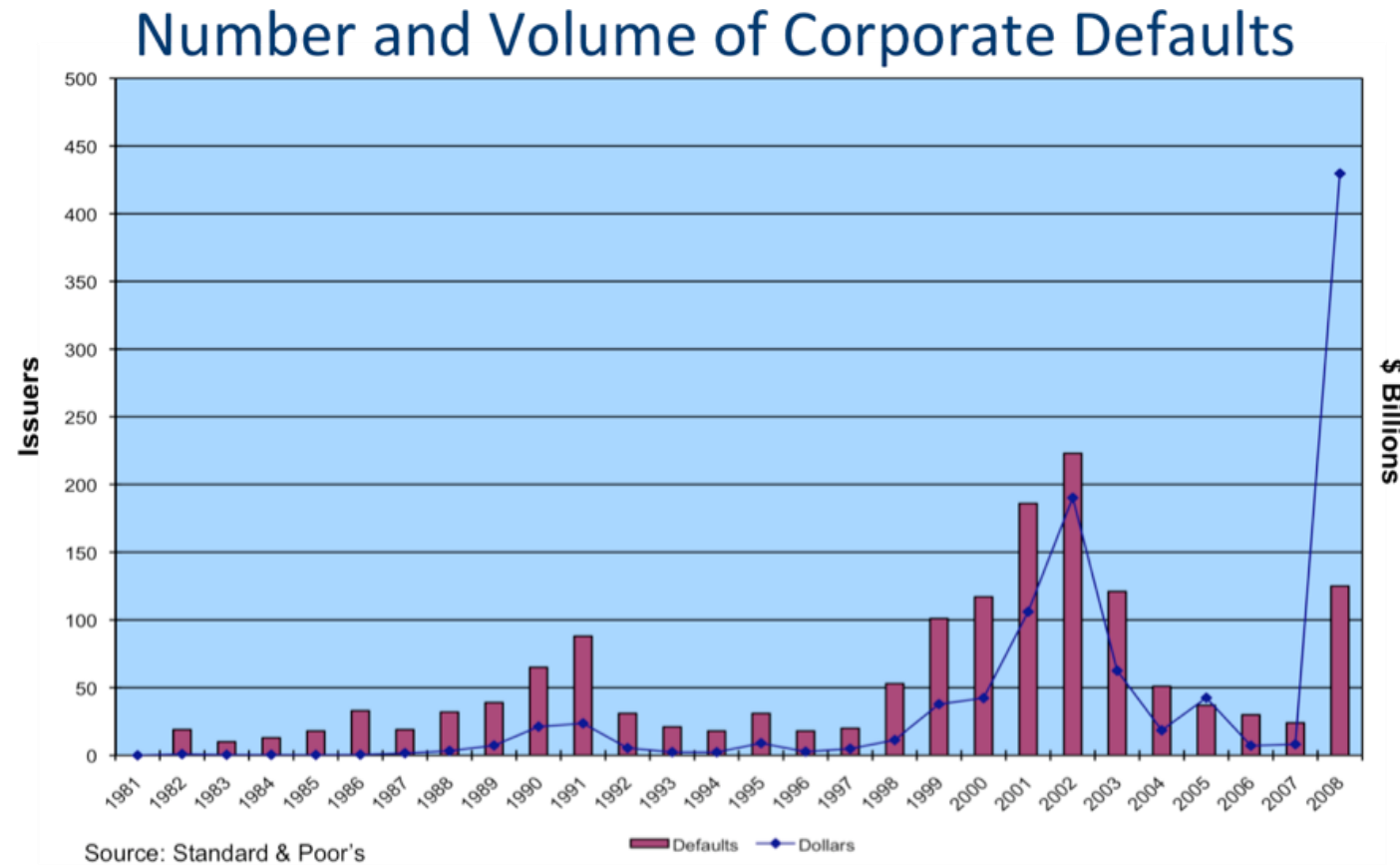
# I. The Gathering Storm of Economic Downturn and Increased Corporate Defaults That Can Cause Further State and Local Government Financial Distress

Mergers and Acquisitions Completions Compared to Corporate Default Rates (including mergers, acquisitions and divestitures priced at \$5 million and over) (US)



Source: M&A Data: Thomson Financial

# I. The Gathering Storm of Economic Downturn and Increased Corporate Defaults That Can Cause Further State and Local Government Financial Distress



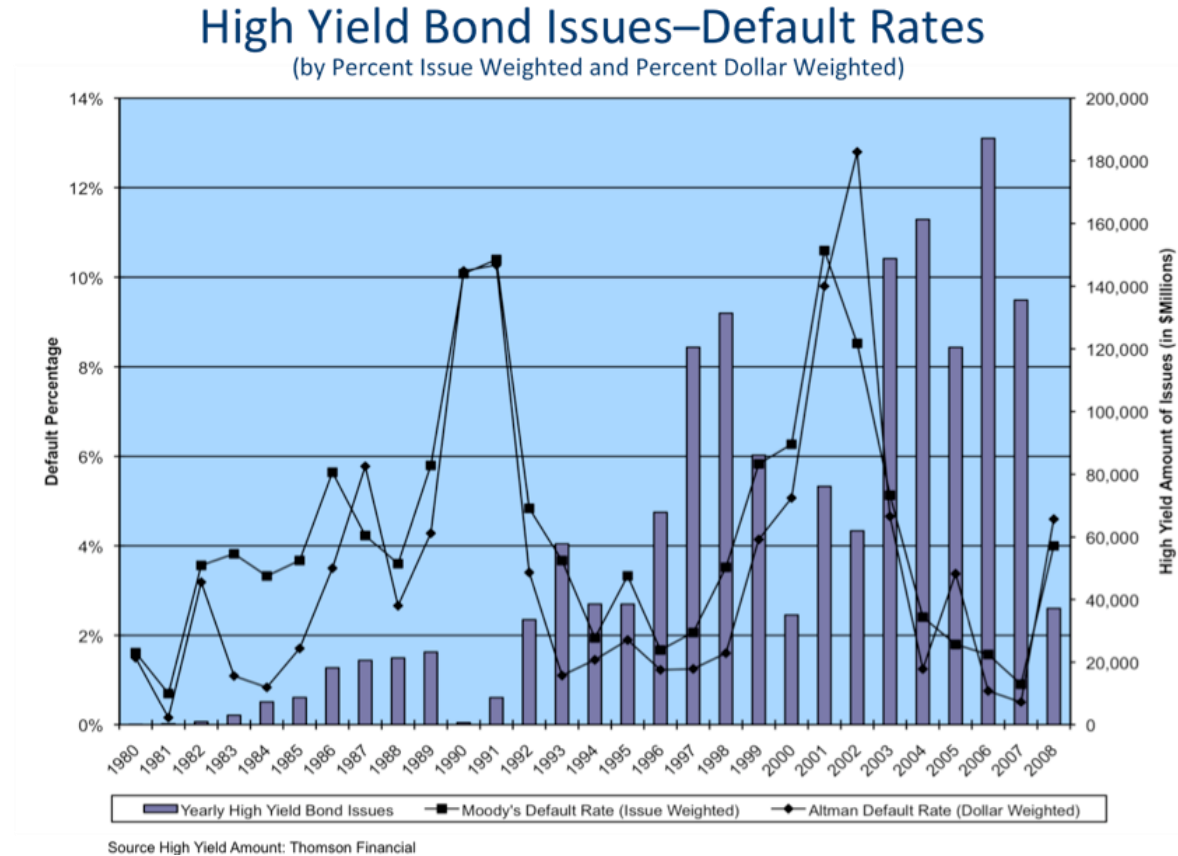
# **I. The Gathering Storm of Economic Downturn and Increased Corporate Defaults That Can Cause Further State and Local Government Financial Distress**

---

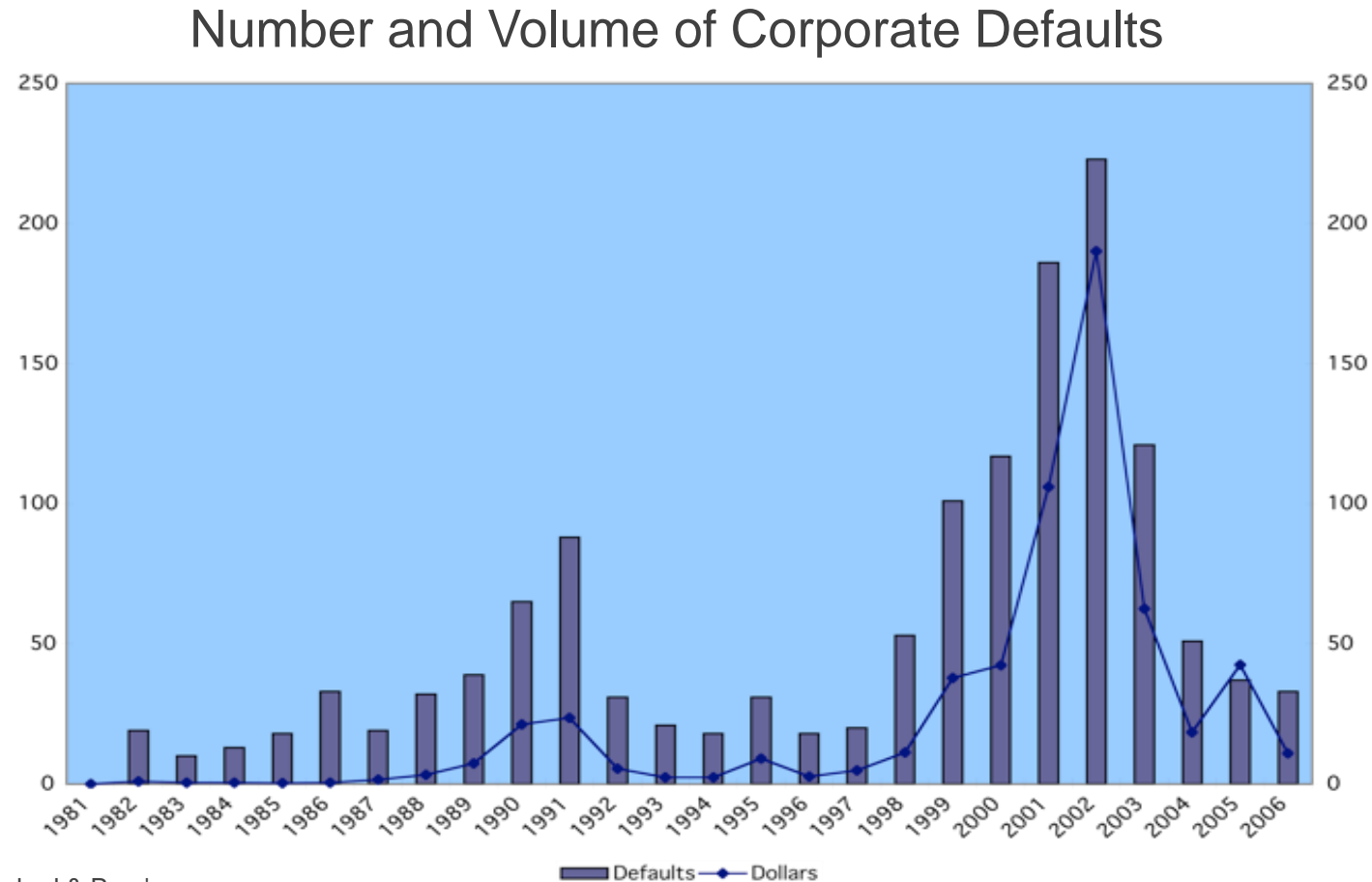
(c) Peak in high-yield (speculative grade) debt issuance:

- In 2006, \$187 billion of high yield debt (speculative grade) was issued in the United States – an all time high.
- In the first half of 2007, over 70% of new bond market issuances were speculative grade, an all time high. This was followed by a peak in corporate defaults in 2008. This was up from 24.4% in 1990 and 50% in 2000 before the peak in corporate defaults in 1991 and 2002.
- High yield U.S. bond debt issuances from 2018 YTD to 2019 YTD (May 2018 and 2019) increased 65.9% from \$64.3 billion to \$106.8 billion. Likewise, will increased corporate defaults follow in the next 12 to 24 months?

# I. The Gathering Storm of Economic Downturn and Increased Corporate Defaults That Can Cause Further State and Local Government Financial Distress



# I. The Gathering Storm of Economic Downturn and Increased Corporate Defaults That Can Cause Further State and Local Government Financial Distress



Source: Standard & Poor's



# I. The Gathering Storm of Economic Downturn and Increased Corporate Defaults That Can Cause Further State and Local Government Financial Distress

---

- (d) Low percentage of loan loss reserves to total loans outstanding at a time of increased loans and credit outstanding:
- Loan loss reserves to total loans outstanding for all banks went from 3.7% for the first quarter of 2010 to 1.19% in the second quarter of 2019 within 0.03% of the 35-year low of 1.16% in the fourth quarter of 2006 just before the Great Recession.
  - Bank credit for all commercial banks went from \$8.939 trillion in June 9, 2010 (with the highest in the prior 37 years being \$9.22 in October 22, 2008) to \$13.456 trillion in June 19, 2019, an increase from the high between 1973 and 2010 of 46% in 2019.
  - Consumer debt rose to \$13.54 trillion in the fourth quarter of 2018 and is now \$869 billion higher than previous peak of \$12.68 trillion in the third quarter of 2008 and 21.4% above the post-financial crisis low in second quarter of 2013.

# **I. The Gathering Storm of Economic Downturn and Increased Corporate Defaults That Can Cause Further State and Local Government Financial Distress**

---

- A low percentage of net charge-off of loans on all loans for all banks has been a sign of economic downturn. Net charge-off of loans on all loans for all commercial banks in the first and second quarter of 2019 was .47% from a 30-year high of 3.14% in the fourth quarter of 2009 to a 30-year low of .34% in the first quarter of 2006 before the Great Recession.
- Corporate debt in USA has risen \$5 trillion in the last 11 years to \$9 trillion. At all time high while cash-on-hand to debt for corporations is at post-financial crisis low (especially not counting the top 25 corporations with cash).
- There is over \$2 trillion of U.S. corporate debt maturing in the next five years. There is 30% of speculative grade and 31% of investment grade debt coming due with less liquidity and bank credit available to refinance it.
- Is the climate right for the next debt tsunami storm?

# I. The Gathering Storm of Economic Downturn and Increased Corporate Defaults That Can Cause Further State and Local Government Financial Distress

---

(e) The ability to predict an economic downturn:

- Impending economic downturns can be predicted by the convergence of a (1) low point of percentage of loan loss reserves to total loans outstanding, (2) rapid increase in mergers and acquisitions. (3) a peak in the issuance of speculative rated debt, dramatic increase in loans and credit, (4) low percentage of net charge-off of loans on all loans for all banks, and (5) inverted yield curve.
- The result of this financial mix is less liquidity and bank credit available when it is needed most resulting in increased defaults with corporate financial meltdown.
- The next big wave of defaults will provide a unique opportunity when valuations crash for those who are prepared to deal with the meltdown. That preparation will predict the winners and losers and the ebb and flow of value in the inevitable financial restructuring.

# I. The Gathering Storm of Economic Downturn and Increased Corporate Defaults That Can Cause Further State and Local Government Financial Distress

## B. Who will feel the adverse effects of the economic downturn?:

1. The problem of cash flow debt in a liquidity crisis. Tight credit and liquidity crisis will affect cash flow dependent financing such as securitization, CDO, ABS, RMBS, SWAPs, credit default SWAPs and derivatives.
2. Reduced bank credit available. Limited ability to lend by bank and financial institutions will affect corporate bond refinancing – \$2 trillion of U.S. corporate bonds maturing in the next five years.
3. What about municipal bonds? The financial distress of corporate and individual taxpayers means less ability to pay taxes and less tax revenue due to less corporate and individual income as well as sale of goods and services to tax. With cost of government services already increasing faster than government revenues, this stresses the state and local governments when current financial health is threatened by unfunded pension liabilities of \$1 to \$3 trillion and needed infrastructure improvements of \$4.6 trillion. This at time already appears insurmountable for some state and local governments.

## II. Need for Timely and Complete Continuing Disclosure on Material Events during Financial Distress of State and Local Government

---

- A. The panic of financial distress can be reduced or eliminated by full and prompt disclosure of the financial situation and the evolving situation:
1. Accurate disclosure. Disclosure should not be overly optimistic or pessimistic as to the situation and alternatives.
  2. Timely disclosure. Delayed disclosure of material events in the hope that there soon will be good news to offset the bad is not helpful.
  3. Historically lower default rates and bankruptcy. The historic lower default rate for rated and nonrated public debt compared to corporate debt should motivate all to at the first signs of financial distress encourage through disclosure a better understanding of the situation and the possible resolution as opposed to rushing into panic mode. See Section III below.

## II. Need for Timely and Complete Continuing Disclosure on Material Events during Financial Distress of State and Local Government

- B. Use of early warning signs. Various indicators of financial distress used in state statutes and credit analysis for detection of a trigger revealing financial distress have been developed. There is no magic formula and the use of indicators, red flags or triggers generally is dependent on the issuer and its unique credit position. Therefore, any early warning sign should be finely tuned to the credit. The following are some of the more commonly used indicators of financial distress:
1. past due debt obligations or judgments of more than a specified percentage of the annual revenues of the local government that have been unpaid for more than six months without an agreement by the creditors to forbear or standstill as to prosecution of the claims;
  2. failure to make statutory or annual required contributions (or a suitable similar substitute concept) to pension funds from existing operating revenues for two consecutive years;

## **II. Need for Timely and Complete Continuing Disclosure on Material Events during Financial Distress of State and Local Government**

---

3. funded ratio for an individual pension plan falls below a specified threshold;
4. failure to pass a budget by a date established after the start of the fiscal year;
5. bills of a specified percentage of annual current revenues as established are left unpaid for a period greater than 180 days, as defined by a payment period;
6. failure to maintain at least 30 days cash on hand in the general fund at the end of the fiscal year for two consecutive years;
7. debts or judgments that are past due for more than six months or pension liabilities exceed a given percentage of the fair market value of taxable real property in the taxing district;
8. financial statements are not published within six months of the close of the fiscal year;

## II. Need for Timely and Complete Continuing Disclosure on Material Events during Financial Distress of State and Local Government

---

9. the unit of local government has defaulted on debt securities;
10. the sum of the annual required contributions and the annual debt service on any outstanding pension obligation bonds has exceeded a threshold (a specific percent of annual revenues) for the last three consecutive years; and
11. any other criteria necessary to determine financial distress of a local government such as:
  - Asset Sufficiency Ratio, which indicates whether the municipality's total assets are adequate to cover all of its obligations or amount owed. It divides general fund total assets by general fund total liabilities. The warning indicator is a consistent deficit in assets' adequacy to meet obligations over the three-year period.



## II. Need for Timely and Complete Continuing Disclosure on Material Events during Financial Distress of State and Local Government

- Debt Burden Ratio, which indicates whether the municipality's annual revenue will cover its annual debt payments, including principal and interest. This ratio divides total government revenue of funds paying debt by the total government debt payments. The warning indicator is when annual revenues consistently are below the annual debt payment for each of the three years.
- Operating Reserve Ratio, which indicates the municipality's reserve to cover future expenditures. This ratio divides the fund balance of the general fund by total general fund expenditures (net of transfers) . The warning indicator is when a reserve that covers less than one week of future expenditures, which is the equivalent of 0.0192 or 1/52, for each of the three years.
- Operating Margin Ratio, which indicates the amount added to the municipality's reserves for every \$1 generated in revenue. This ratio subtracts general fund total expenditures (net of transfers) from general fund total revenue and divides by general fund total revenue. The warning indicator is a loss in reserves for each of the three years.

## II. Need for Timely and Complete Continuing Disclosure on Material Events during Financial Distress of State and Local Government

- Deficit Fund Balance Ratio, which indicates the portion of annual revenue the municipality must generate simply to cover an existing deficit fund balance in a government fund. This ratio is only calculated when a net deficit fund balance exists. This ratio subtracts the fund balance of the general fund, if the balance is positive, from the total deficit fund balances (shown as an absolute value) and divides the total by the total revenue in the deficit funds. The warning indicator is the portion of annual revenue needed to cover the deficit fund balance is increasing over the three-year period.
- Change in Fund Balance Ratio, which indicates whether the municipality's reserves in its general fund are increasing or decreasing. This ratio subtracts the prior year fund balance of the general fund from the current year fund balance and divides by the prior year fund balance. The warning indicator is consistent decreases in revenues.

These criteria are examples of indicators that can be further refined and expanded. Some indicators and triggers should be adjusted for the particular governmental credit. Perhaps there could be developed a list of local governments designated by green light no red flag indicators, yellow lights less than two red flag indicators and red light three or more red flag indicators.

## II. Need for Timely and Complete Continuing Disclosure on Material Events during Financial Distress of State and Local Government

- C. Use of "better" financial reporting models. There should be consideration of having the financial information for state and local government reported under extensible Business Reporting Language ("XBRL") or a municipal credit equivalent that would enable market participants to more easily pull and process data about government finances, including pension from a centralized database as compared to a pdf CAFR. For about the last ten years, XBRL has been used by corporations for SEC filings. See Marc Joffe article on municipal use of XBRL at the following link:

<https://www.alec.org/article/joffe-florida-leads-the-way-on-budget-transparency-with-municipal-xbrl/>

Also, there is the question of whether GASB should be modified by requiring full-accrual accounting in addition to current-fund accounting or separate and in place of it. Accrual accounting would short all liabilities including pension and OPEB, especially on a current basis.

## II. Need for Timely and Complete Continuing Disclosure on Material Events during Financial Distress of State and Local Government

---

D. Tell one tell all is the best practice:

1. While everyone will be inquiring, it is always better to tell all investors publicly.
2. If strategically certain information is sensitive, then consider, for those investors who desire it, non-disclosure confidentiality agreement with recognition of the restriction on trading that is required by the law.

E. Disclosure may be the workout or resolution's best friend:

1. Disclosure allows all to understand the situation including those who would constructively help if they knew the accurate situation.
2. The state and others who have an interest in the long term financial survival of the local government cannot offer help or solutions if they do not know the full accurate financial situation.

## II. Need for Timely and Complete Continuing Disclosure on Material Events during Financial Distress of State and Local Government

- F. Checklist of disclosures to maximize market acceptance in evaluating repayment of bond debt and to help bondholders and trustees in asserting their rights and interests:
1. Authorized to file Chapter 9? Can the issuer file for Chapter 9, if not, then right to enforce obligation in state court by mandamus and other remedies without a required restructuring?
  2. What is source of payment? Is the general obligation debt a "naked" full faith and credit promise or does it have a pledge of special revenues or statutory lien pledging and dedicating a specific and adequate tax revenue source for payment. (Alexander Hamilton in the 1790s said the secret of making public credit "immortal" is that whenever public debt is increased, it ought to be accompanied by a sufficient tax increase dedicated to its payment. (Syrett, The Papers of Alexander Hamilton, Vol. 6, p. 106 and Vol. 18, p. 103).).
  3. Is there a lack of diversification of tax sources and limits on taxes that could realistically be triggered? Are sources of tax revenues too limited or are there tax limits and debt limits close to being triggered that may prevent the raising of taxes to pay the obligation?

## II. Need for Timely and Complete Continuing Disclosure on Material Events during Financial Distress of State and Local Government

4. Are there required priorities, set asides or appropriations to support payment? Do state constitutions or statutes provide for a priority of payment for general obligation debt or mandatory set aside of revenues or appropriations for payment of the debt? (Can plan of debt adjustment be confirmed if it is not in compliance with state law by not permitting mandatory priority of payment, set asides or appropriations? Could be a real obstacle to confirming a plan.)
5. Are there effective remedies available if there is a default? Do the state statutes and case law provide effective remedies (mandamus, intercept, constitutional or statutorily required set asides, priority of payment, or appropriation) and does state court effectively enforce them?
6. Is effective state oversight and assistance available to prevent defaults or aid a financially troubled municipality? Does the state provide by statute or practice the ability to monitor and oversee a financially challenged municipality, provide financial guidance and support to bridge the economic downturn and avoid litigation meltdown and Chapter 9.

### III. Need to Educate the Municipal Market as to the Myth and Reality of Financial Distress of State and Local Governments Through Enhanced Disclosure

---

- A. Undisputable need for full, clear and accurate disclosure of the financial conditions and resolution alternatives of a distressed issuer:
1. A level playing field: Adequate disclosure, education and understanding of the realities of government financial distress will level the playing field and insure transparency so that investors are on equal footing with respect to the basics of the situation.
  2. Effective and efficient market: The better, the clearer, the more accurate the disclosure, education and understanding of the market, the more efficient and effective the market will be.

### III. Need to Educate the Municipal Market as to the Myth and Reality of Financial Distress of State and Local Governments Through Enhanced Disclosure

---

- B. The challenge of municipal disclosure: With regard to State and Local Government debt financing, there are a number of relevant facts concerning the status of the municipality when and if it faces significant financial distress that should be understood:
1. What is the risk of default or Chapter 9 bankruptcy?
  2. Whether Chapter 9 bankruptcy is authorized by the state?
  3. What is the source of payment of special revenues, statutory liens or other protected payment in a Chapter 9?
  4. Are there diversity of tax sources and limits on taxes and debt that enhance the ability of the municipality to pay?
  5. Is there effective state oversight and assistance available to prevent defaults, avoid financial meltdown and aid a financially distressed municipality?



### **III. Need to Educate the Municipal Market as to the Myth and Reality of Financial Distress of State and Local Governments Through Enhanced Disclosure**

---

6. Has underfunding of pension and OPEB obligations as well as deferred needed infrastructure improvements been adequately disclosed and will funding of these obligations crowd out funding for essential services?
7. Has continuing disclosures of material events been timely and complete during the period of financial distress?

### III. Need to Educate the Municipal Market as to the Myth and Reality of Financial Distress of State and Local Governments Through Enhanced Disclosure

---

- C. Education of and disclosure to the market and investors is essential: This presentation is intended to encourage the education and, if appropriate, disclosure of the factual answers to the questions posed in paragraph 3 above and the development of data criteria and triggers to warn of impending financial crisis. The purpose is not to expand required disclosure as much as to encourage voluntary disclosure made in good faith to help the market and investors better understand and assess the distressed situation. It is hoped that the reward for such additional disclosure use of standardized criteria will be the basis for greater market credibility and acceptance and better credit ratings. Further, there should be a safe harbor for such good faith attempts to assist the market with such disclosures due to the dynamic uncertainty of financial distress situations. The following will be a review of the factual and legal background material relating to the answers to the questions set forth in paragraph 3 above.

## IV. The Historic Risk of Financial Distress and Bankruptcy of Issuers in the Municipal Market

---

- A. Historical default rate: Default rate for state and local government debt has been relatively low especially when compared to corporate debt default:
1. Historically, while political risk of non-payment was a possibility, it was a rare occurrence, if not in reality a non-existent concern, with a few exceptions (*i.e.* 8 States and one Territory repudiated their debt between 1841 to 1843 with 7 of the 9 resuming payment by 1849, repudiation of Civil War related debt by 8 states in the late 1860's, railroad bond and real estate defaults of the 1870s to 1890s and Washington Public Power Supply System, 1983). There are current situations that may test the long-term viability of the historical premise. Namely, it is hoped that Puerto Rico, Detroit, Stockton, San Bernardino and Jefferson County are rare aberrations rather than indicative of a growing trend.

## IV. The Historic Risk of Financial Distress and Bankruptcy of Issuers in the Municipal Market

---

2. Between 1939 and 1969 there were 6,195 recorded defaults of municipal issues:
  - (a) The defaults between 1939 and 1969 consisted of default by 727 counties and parishes, 1,911 incorporated municipalities, 313 unincorporated municipalities, 1,372 School Districts and 1,872 special purpose districts.
  - (b) During the period of 1929-1937 there were 4,770 defaults by Governmental Bodies consisting of the following: From 1839-1969 there were only 6,195 municipal bond defaults for 81,248 local government for an annual average default rate of .058%.

# IV. The Historic Risk of Financial Distress and Bankruptcy of Issuers in the Municipal Market

## Recorded Defaults, by Type of Local Government Unit 1839-1969

	1839 -49	1850 -59	1860 -69	1870 -79	1880 -89	1890 -99	1900 -09	1910 -19	1920 -29	1930 -39	1940 -49	1950 -59	1960 -69	Total Defaults	Number of Local Governments in 1967 <sup>a</sup>	% of Annual Default Rate Over 130 Yrs. <sup>b</sup>
By Type of Units																
Counties and parishes		7	15	57	30	94	43	7	15	417	6	12	24	727	3,049	.183%
Incorp. munics.	4	4	13	50	30	93	51	17	39	1,434	31	31	114	1911	18,048	.081%
Unincorp. munics.		4	9	46	31	50	33	5	10	88	7	4	26	313	17,105	.014%
School districts				4	5	0	11		14	1241	5	23	60	1,272	21,782	.048%
Other districts				2	1	12	11	7	107	1,590	30	42	70	1,872	21,264	.067%
<b>Totals</b>	<b>4</b>	<b>15</b>	<b>37</b>	<b>159</b>	<b>97</b>	<b>258</b>	<b>149</b>	<b>36</b>	<b>185</b>	<b>4,770</b>	<b>79</b>	<b>112</b>	<b>294</b>	<b>6,195</b>	<b>81,248</b>	<b>.058%</b>

<sup>a</sup> The number of local government units has changed rapidly. For example, in 1932 there were 127,108 school districts, 8,580 other districts, and 175,369 state and local government units.

<sup>b</sup> The percent of annual default in total defaults by type divided by number of governments divided by 130 (years).

Sources: Default information in *The Daily Bond Buyer*, *The Commercial and Financial Chronicle* and *The Investment Bankers' Associations Bulletin*; default lists from Federal Deposit Insurance Corporation, Life Insurance Commission, and U.S. Courts; and Albert M. Hillhouse, *Defaulted Municipal Bonds* (Chicago: Municipal Financial Officers Association, 1935). Number of local government units from: U.S. Department of Commerce, Bureau of Census, Census of Governments, 1967, Vol. 1 "Governmental Organization" (Gov't Printing Office, 1969) and ACIR Report Bankruptcy, Defaults and Other Local Government Financial Emergencies U.S. Government 1973.

## IV. The Historic Risk of Financial Distress and Bankruptcy of Issuers in the Municipal Market

---

See: A Commission Report "City Financial Emergencies: The Intergovernmental Dimension", Advisory Commission on Intergovernmental Relations, Washington, D.C., July, 1973.

3. During the 1930's municipal units defaulted in the payment of interest or principal on some 10% of the then outstanding total of \$15 billion of municipal bonds. Between 1945 and 1970 Municipal Bonds in the principal amount of \$450,000,000 went into default which constituted .4% of the principal amount of Municipal Bonds outstanding in 1970.

## IV. The Historic Risk of Financial Distress and Bankruptcy of Issuers in the Municipal Market

---

- B. Recent default rate: Historically, there is a low default rate for bonds issued by municipalities and studies of recent default since 1970 continue the trend:
1. The late Dr. John Petersen of George Mason University noted in his paper on "Municipal Defaults: Eighty Years Made a Big Difference" (2011) that, between 1970's-2000's, the municipal default for municipalities averaged per decade .10% to .24% (adjusted for WPPSS and Jefferson County, Alabama) not including the fact that over 80% of the defaults were conduit financings and not essential public financings. This is a far cry from the corporate bond default rate on average for investment grade and non-investment grade of about 10%. (Petersen, 2013).
  2. States have not defaulted on general obligations bonds since the late 1880's, with the exception of Arkansas debt in 1933, which was thereafter refinanced.

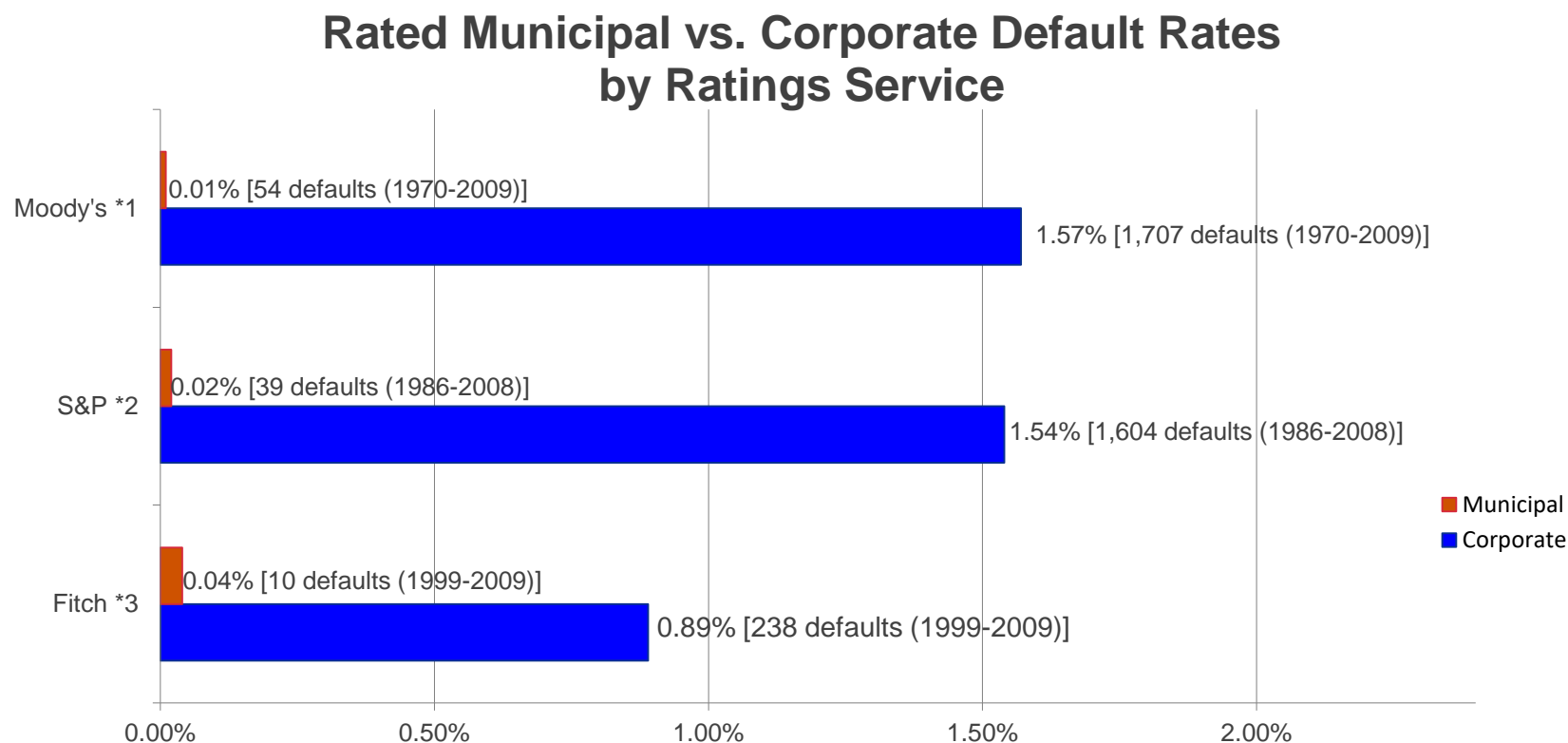
## IV. The Historic Risk of Financial Distress and Bankruptcy of Issuers in the Municipal Market

---

3. Historically, based on default rate, there is little support for the willingness to pay to be deemed a real problem since there is an absence of political risk.
4. Essential service debt financing has historically enjoyed a significantly lower default rate than healthcare, housing and conduit state and local governmental financing.
5. Unfunded pension obligations and deferred infrastructure costs are a more recent phenomenon – Prior to 1960s, most pension obligations were treated as gratuities and a significant number of big ticket infrastructure costs are only now starting to age such as the interstate highway system, electric grid, waste water treatment facilities, etc.
6. We are closer to a tipping point and departure from the historical assurances than we have ever been. The difference may be whether there will be adherence to the Washington-Hamilton principle of honoring the payment of public debts and reinvesting in state and local government going forward.



# IV. The Historic Risk of Financial Distress and Bankruptcy of Issuers in the Municipal Market



1. Moody's Investors Services, U.S. Municipal Bond Defaults and Recoveries, 1970-2009 (February 2010); Moody's Investors ServCorporate Default and Recovery Rates, 1920-2009 (February 2010). Percentages based upon average one-year default rate.
2. Standard & Poor's, 2009 Global Corporate Default Study and Ratings Transitions (March 17, 2010); Standard & Poor's; U.S. Municipal Ratings Transitions and Defaults, 1986-2009 (March 11, 2009). Percentages based on average default rate.
3. Fitch Ratings Inc. U.S. Public Finance Transition and Default Study (1999-2009), March 25, 2010; Fitch Ratings Global Corporate Finance 2009 Transition and Default Study.

## IV. The Historic Risk of Financial Distress and Bankruptcy of Issuers in the Municipal Market

- C. U.S. municipal defaults and recovery 1970-2013: Moody's report on U.S. Municipal Defaults and Recovery 1970-2013 further supports a lower default rate and higher recovery than on corporate bonds and found:
1. Municipal bond defaults for rated bonds remain extremely low namely 1.3 defaults per year on average between 1970-2007 period (0.01%) and 5 defaults per year from 2008-2013 period (7 in 2013 and 5 in 2012 with an average of 5 defaults) or 0.03%. Between 1970-2015, there were 99 defaults of rated municipal bonds over 46 years, an average of just over 2 per year.
  2. The ultimate recovery rate remains higher than on corporate defaults with at least 60% recovery for the 1970-2013 period for municipal rated bonds versus 48% recovery for corporate senior unsecured rated bonds. Ranges vary by case – Jefferson County at least 80% for sewer bonds class, 100% of principal for G.O. warrants: Vallejo, Sierra King - 100% recovery for special revenues.
  3. S&P Global Ratings has similar findings as noted in its 2017 Annual U.S. Public Finance Default Study and Rated Transaction.

## IV. The Historic Risk of Financial Distress and Bankruptcy of Issuers in the Municipal Market

---

4. Moody's concentration by sector of municipal defaults from 1970-2011:



## IV. The Historic Risk of Financial Distress and Bankruptcy of Issuers in the Municipal Market

- D. Defaults 2012-2017: Recently, monetary defaults on state and local government public debt ranged from 108 issuers for \$1.95 billion in default in 2012 to 68 issuers for \$8.57 billion in default in 2013 to 58 issuers for \$9.02 billion in default in 2014 to 60 issuers for \$3.93 billion in default in 2015 to 67 issuers for \$27.51 billion in default in 2016 to 43 issuers in default in 2017, the lowest since 2009. (Municipal Market Analytics):
1. While there was a decline in the number of issuers in default by almost 50%, there was however the rise in dollar value of defaults in 2013, 2014 and 2016. This was due to Detroit's filing for bankruptcy and defaulting and a large energy company bankruptcy (2013 and 2014) and Puerto Rico defaults (2016). For example, \$5.4 billion of the \$9.02 billion in default in 2014 were the Detroit water and sewer bonds that ultimately were unimpaired in the plan of debt adjustment. In addition, TXU, a subsidiary of Energy Future Holdings Company, declared bankruptcy in April 2014, which filing caused the default on \$1.16 billion of industrial development bonds. The Puerto Rico COFINA defaults of \$18.18 billion took place in 2016.

## IV. The Historic Risk of Financial Distress and Bankruptcy of Issuers in the Municipal Market

- E. Bankruptcy: Historically the use of Chapter 9 bankruptcy by a municipality has been rare and a last resort especially compared to corporate Chapter 11 filings:
1. Since 1937 when Chapter 9 municipal debt adjustment was enacted over 80 years ago there have been only 684 Chapter 9 filings namely by small municipal utilities and special tax districts and by some cities, towns, villages and counties but generally not of any significant size.
  2. Since 1954, virtually all of those municipalities that filed Chapter 9 were small or not major issuers of bond debt except for Bridgeport, CT in 1991, Orange County in 1994, Vallejo, CA in 2008, Jefferson County, AL in 2011, Stockton and San Bernardino, CA in 2012 and Detroit in 2013. Both Harrisburg, PA and Boise County, ID. cases were dismissed as was Bridgeport in 1991.

## IV. The Historic Risk of Financial Distress and Bankruptcy of Issuers in the Municipal Market

---

3. Of the 315 Chapter 9 filings since 1980 and of the 340 filings since 1954, 183 (208 since 1954) have been municipal utilities and special districts and only 55 (65 since 1954) have been cities, counties, towns and villages. The remaining, 62 (since 1954 and 1980) have been hospitals or healthcare, 8 transportation and 7 school or educational facilities. Less than 70% of the Chapter 9 filings resulted in a confirmed plan of debt adjustment.
4. Since 1980 Chapter 11 corporate filings have averaged at least 10,000 per year compared to about 8.5 Chapter 9 filings per year.

## IV. The Historic Risk of Financial Distress and Bankruptcy of Issuers in the Municipal Market

---

- F. Causes of bankruptcy: Recent causes of Chapter 9 to be noted and financial condition of issuers to be avoided:
1. Deferred costs of capital improvements and infrastructure costs. (Detroit and Central Falls)
  2. The bursting of the local government debt bubble. (Jefferson County and Detroit)
  3. Decline of urban areas. (Detroit and Central Falls)
  4. Proposition thirteen mentality – The popularity of tax caps and limitations. (Stockton and San Bernardino)
  5. Unaffordable and unsustainable personnel costs. (Vallejo, San Bernardino, Detroit)
  6. Lingering legal issues and surprise court decisions. (Town of Mammoth Lakes and Boise County, Idaho)

## IV. The Historic Risk of Financial Distress and Bankruptcy of Issuers in the Municipal Market

---

7. Off balance sheet liabilities. (Underfunded pension obligations – Stockton, San Bernardino, Detroit)
8. Willingness to pay versus ability to pay – Willingness to pay traditionally has not been a problem but could be a growing problem. (Jefferson County, Orange County, etc.)



## IV. The Historic Risk of Financial Distress and Bankruptcy of Issuers in the Municipal Market

### G. Current use of Chapter 9:

1. No Tsunami of Chapter 9 filings in 2012, 2013, 2014, 2015, 2016, 2017 and 2018.
2. Only 13 Chapter 9 filings in 2011, 12 in 2012, 8 in 2013, 10 in 2014, 3 in 2015, 6 in 2016, 6 in 2017, 4 in 2018 and 3 so far in 2019.
3. Only 4 cities, towns, counties or villages filed Chapter 9 (municipal bankruptcy) in 2011, namely Jefferson County, Central Falls, Boise County and Harrisburg, PA (Boise County and Harrisburg were dismissed), 3 in 2012, namely Stockton, San Bernardino and Mammoth Lakes (which was dismissed that year) and only 1 in July, 2013 – namely Detroit. Since the Detroit Chapter 9 was filed in 2013, and, so far in 2019 (almost five years), one city, Hillview, KY in August 2015, filed for Chapter 9 and that was dismissed in April, 2016 without filing a plan of debt adjustment and the City of Perla, Arkansas, filed in 2019, a town with a population of 241, essentially a water association.

## IV. The Historic Risk of Financial Distress and Bankruptcy of Issuers in the Municipal Market

---

4. Total Chapter 9 filings since 1937 – 684.
5. States cannot file Chapter 9.
6. Co-Sovereign with Federal Government and 10<sup>th</sup> Amendment Issues.
7. Chapter 9 filings are still RARE and mainly small special tax districts, municipal utilities.
8. In the last 65 years, only 65 cities, towns, counties and villages have filed out of 340 Chapter 9 filings that have been made. Thirty of the 65 (46%) were Chapter 9 cases dismissed before any plan of debt adjustment was confirmed with purportedly the city, town, village or county found a better resolution or was not authorized to file under state laws.

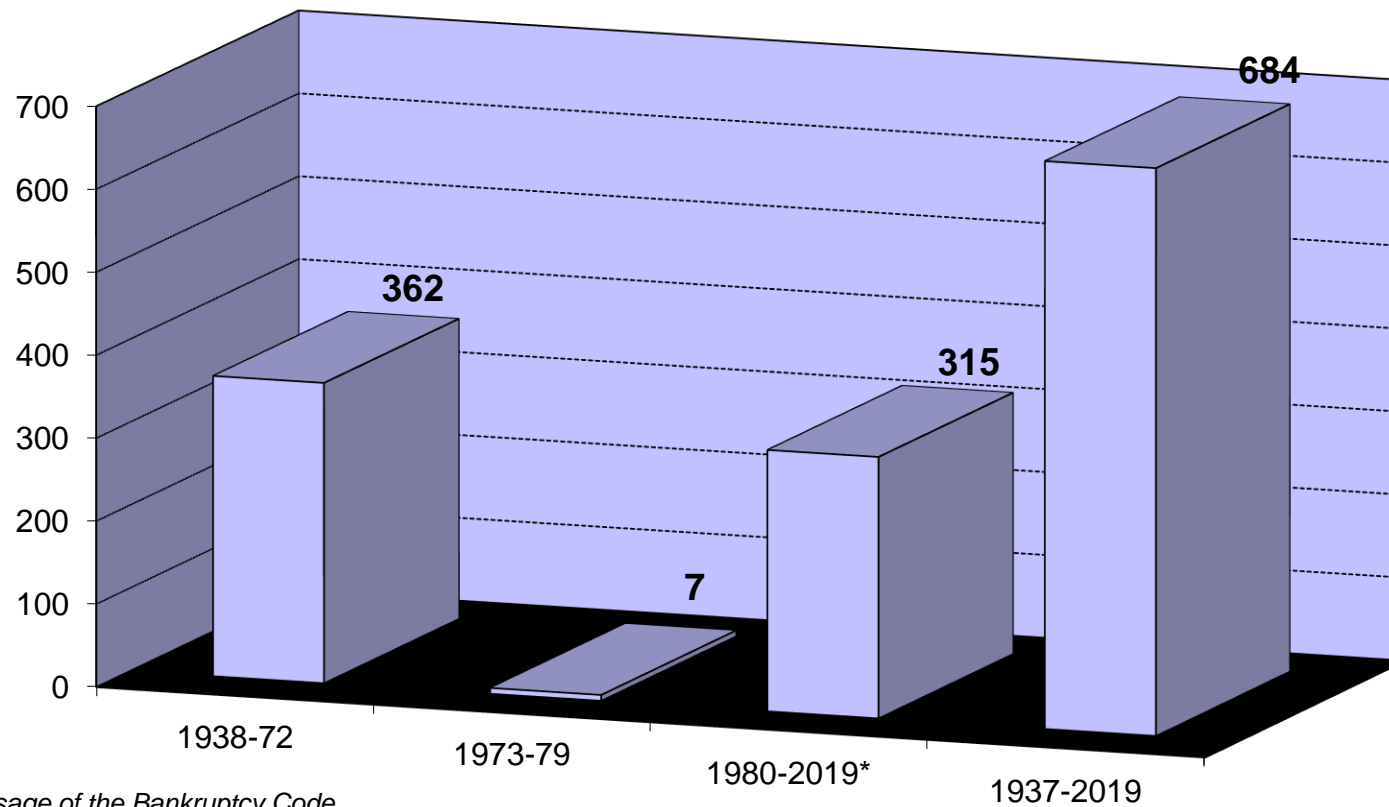
## IV. The Historic Risk of Financial Distress and Bankruptcy of Issuers in the Municipal Market

The largest cities, towns, villages and counties to have filed Chapter 9 bankruptcy in the last 60 years (including Detroit):

	Approximate Population	Approximate Debt in Millions
Orange County (filed 1994)	3,000,000	\$1,974
Vallejo, California (filed 2008)	115,942	\$175 (2008)
Jefferson County (filed 2011)	658,931 (2011)	\$4,200
Stockton, California (filed 2012)	291,707 (2010)	\$1,032 (2011)
San Bernardino (filed 2012)	213,012 (2011)	\$492.3 (2011)
Detroit, Michigan (filed 2013)	701,475 (2012)	\$18,500 (2013)

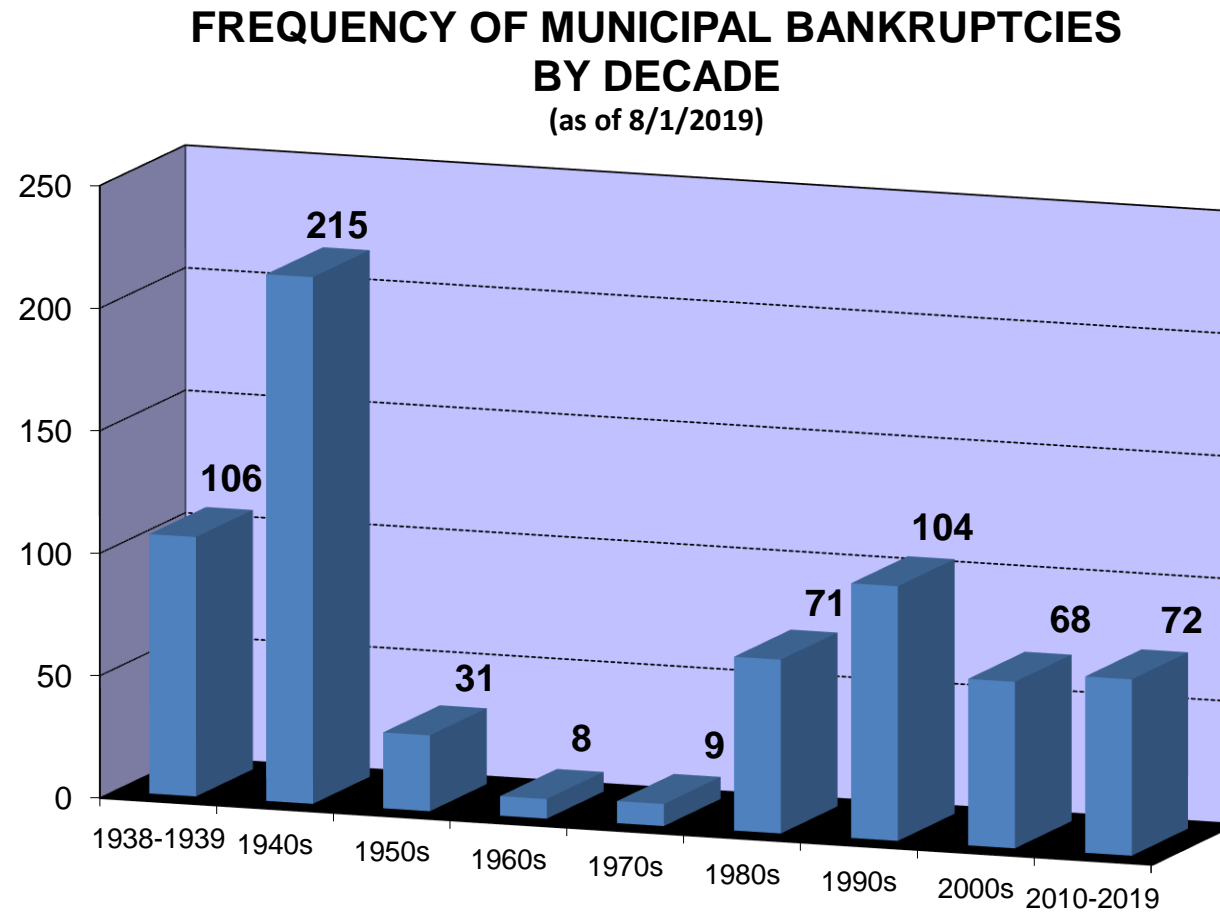
## IV. The Historic Risk of Financial Distress and Bankruptcy of Issuers in the Municipal Market

**FREQUENCY OF MUNICIPAL BANKRUPTCIES • 1937-2019**  
(as of 8/1/2019)

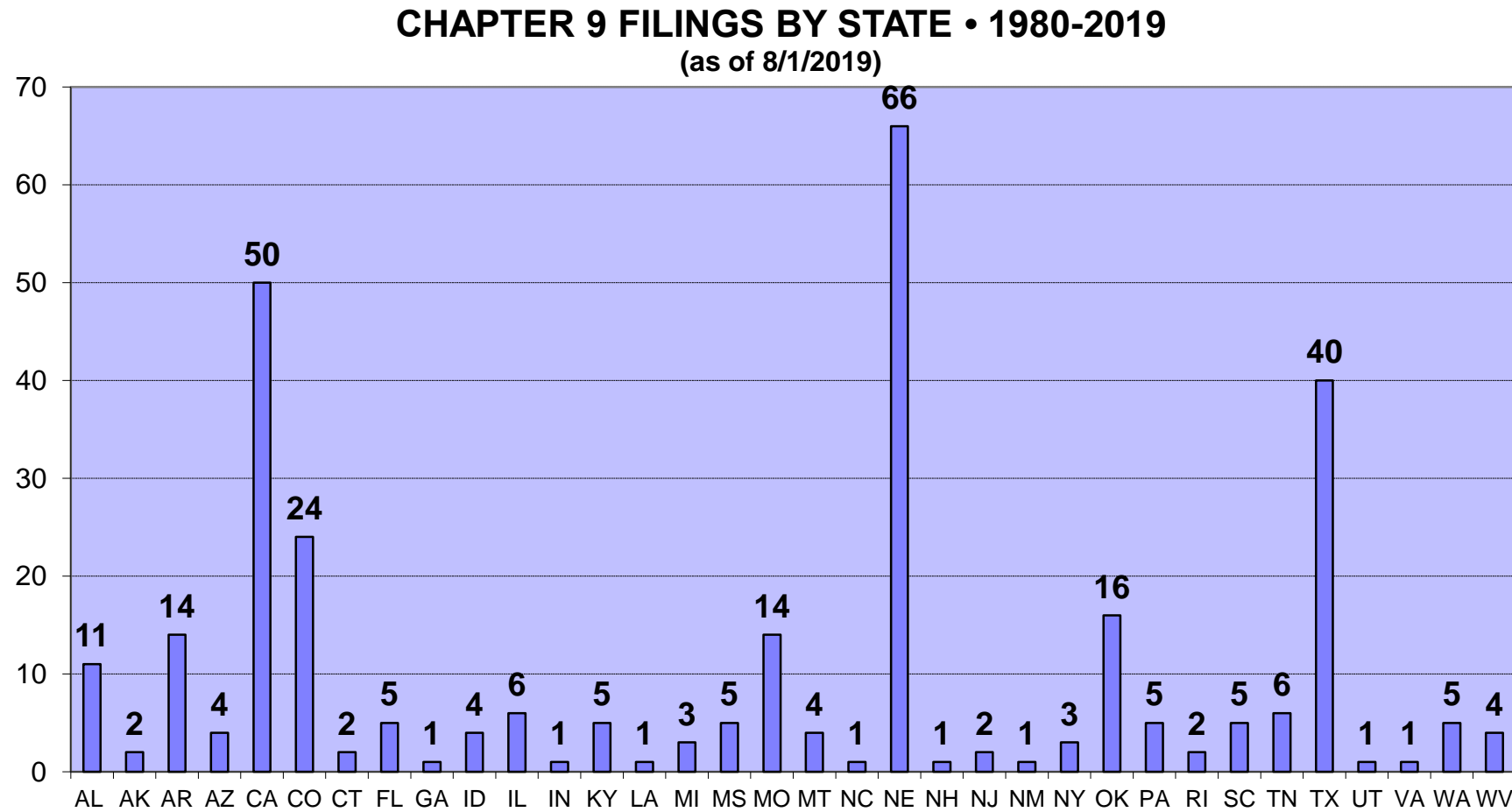


\* Since passage of the Bankruptcy Code.

## IV. The Historic Risk of Financial Distress and Bankruptcy of Issuers in the Municipal Market

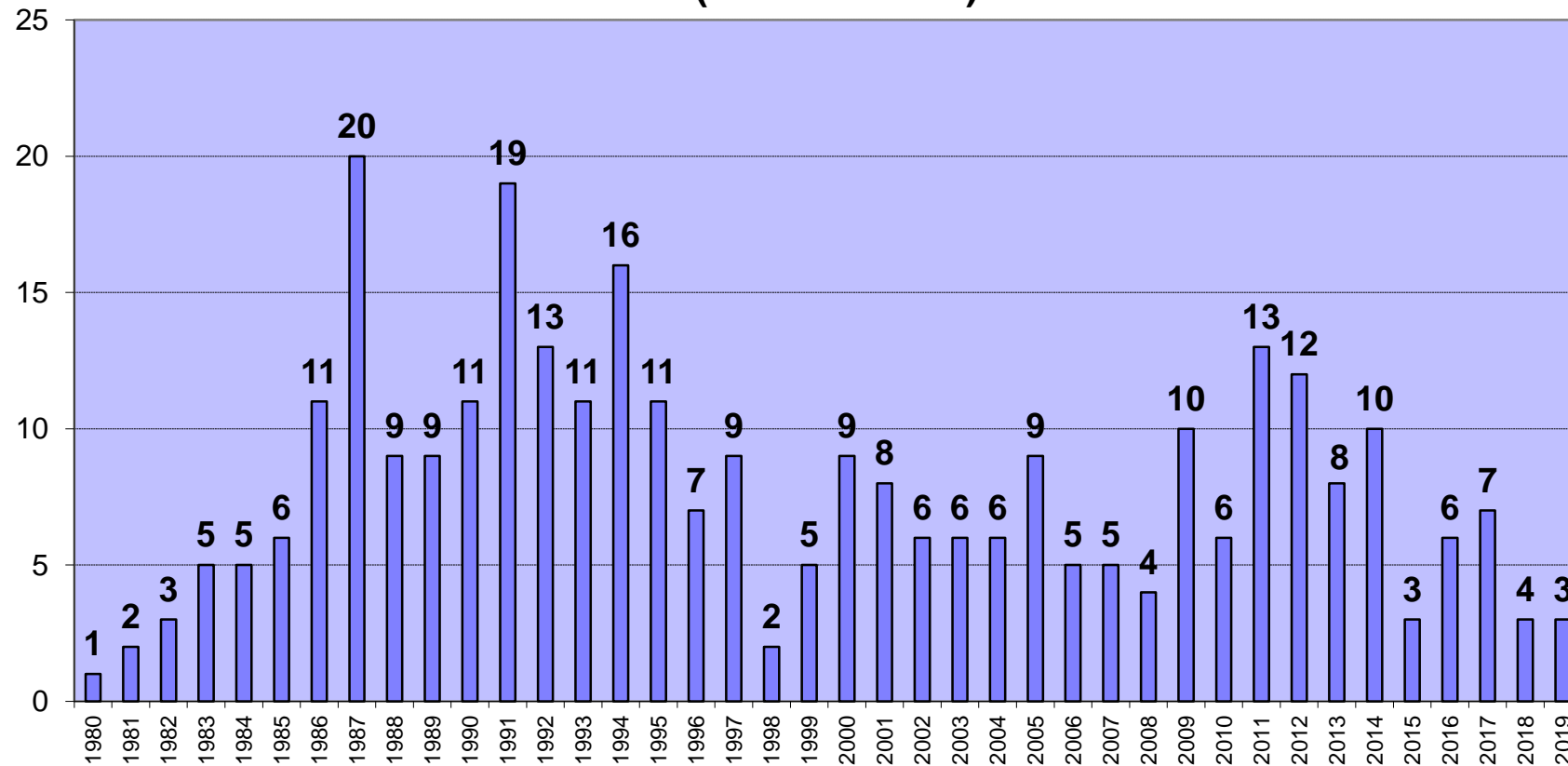


## IV. The Historic Risk of Financial Distress and Bankruptcy of Issuers in the Municipal Market



# IV. The Historic Risk of Financial Distress and Bankruptcy of Issuers in the Municipal Market

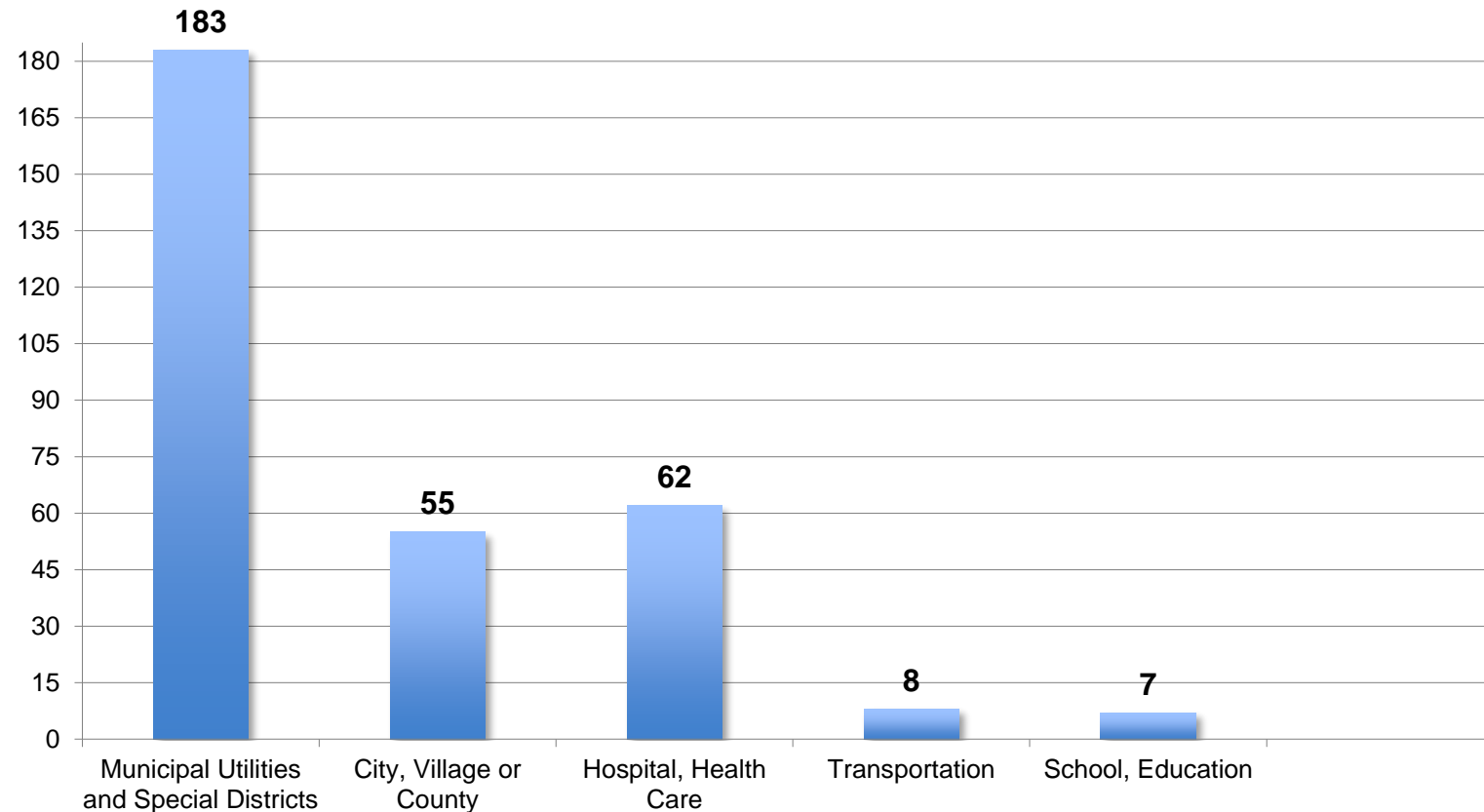
CHAPTER 9 FILINGS BY YEAR • 1980-2019  
(as of 8/1/2019)



## IV. The Historic Risk of Financial Distress and Bankruptcy of Issuers in the Municipal Market

### CHAPTER 9 FILINGS BY TYPE • 1980-2019

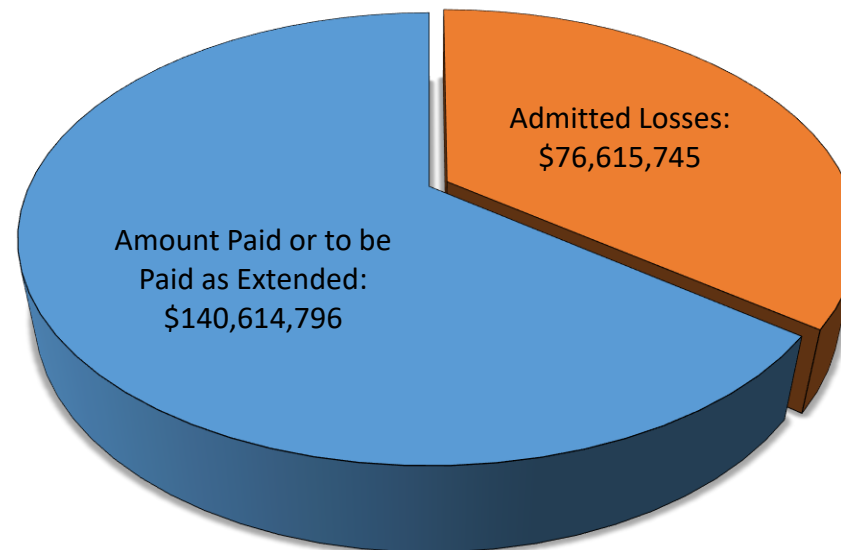
(as of 8/1/2019)





## IV. The Historic Risk of Financial Distress and Bankruptcy of Issuers in the Municipal Market

### MUNICIPAL BANKRUPTCY RECOVERY 1938-1972\*

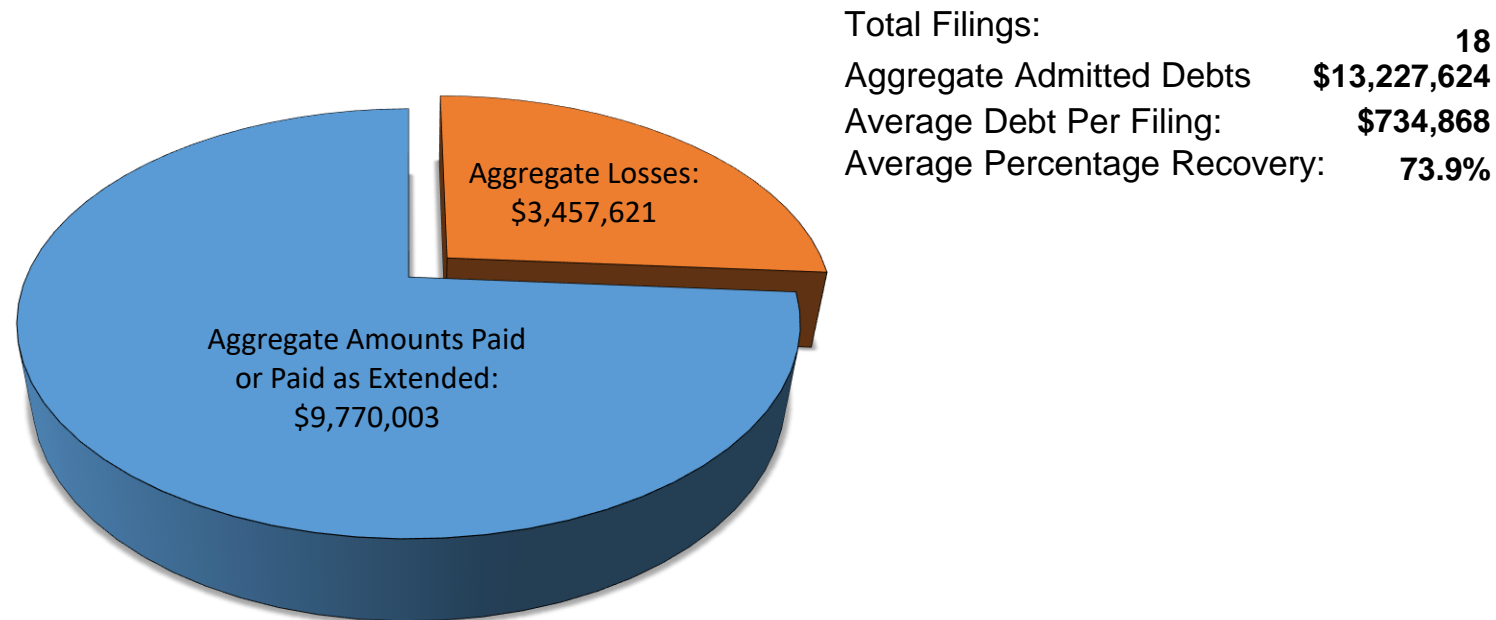


Total Filings: 362  
Aggregate Admitted Debts: \$217,230,541  
Average Debt Per Filing: \$600,084  
Average Percentage Recovery: 64.7%

\* See Table 5-1, *City Financial Emergencies: The Intergovernmental Dimension*, Advisory Commission on Intergovernmental Relations, July 1973.

## IV. The Historic Risk of Financial Distress and Bankruptcy of Issuers in the Municipal Market

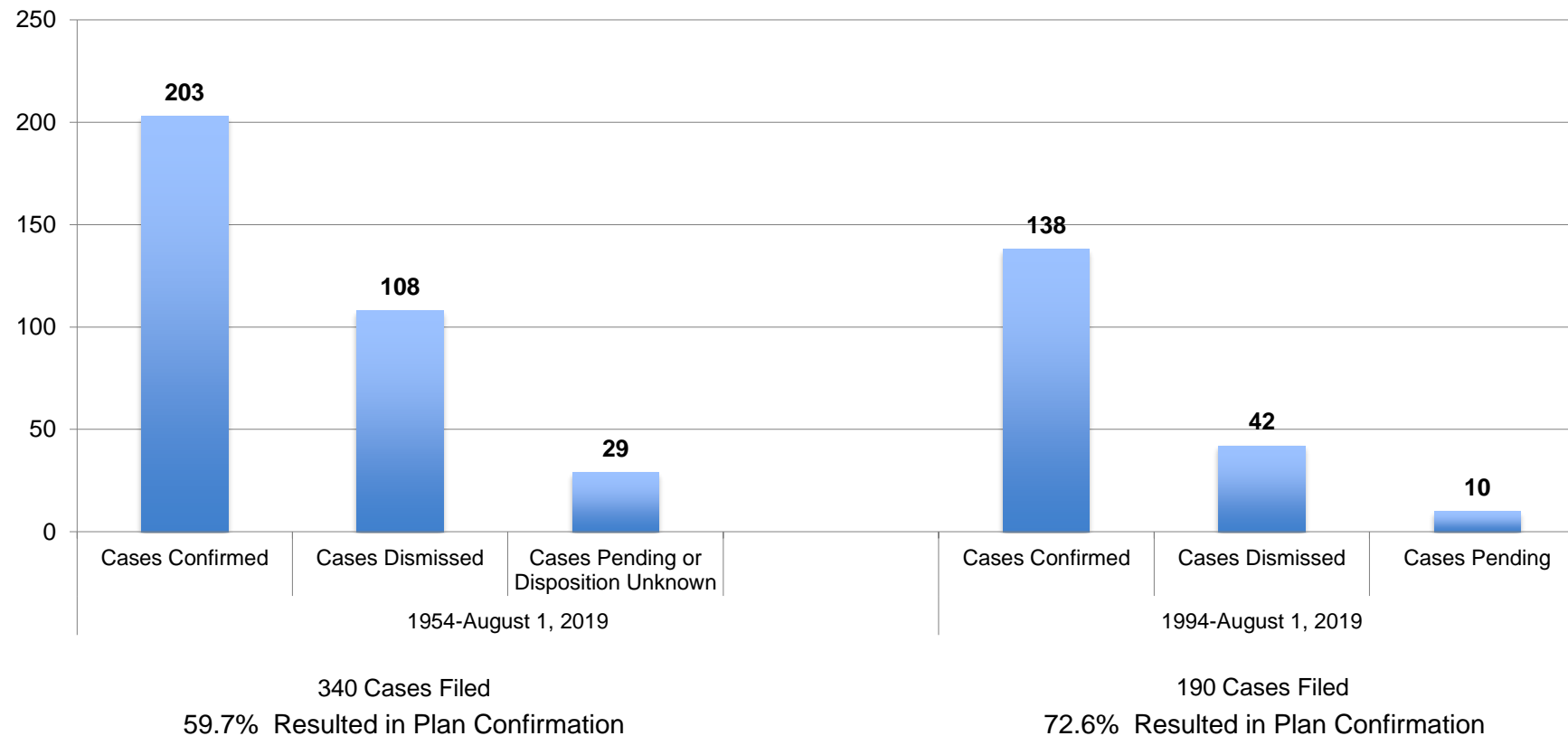
### MUNICIPAL BANKRUPTCY RECOVERY 1954-1972\*



\* See Table 5-1, *City Financial Emergencies: The Intergovernmental Dimension*, Advisory Commission on Intergovernmental Relations, July 1973.

## IV. The Historic Risk of Financial Distress and Bankruptcy of Issuers in the Municipal Market

### DISPOSITION OF CASES



## IV. The Historic Risk of Financial Distress and Bankruptcy of Issuers in the Municipal Market

---

### H. Defaulted municipal bond recovery rates:

#### 1. Historic Chapter 9 recovery rate:

- 1938-1972 period. Chapter 9 recovery rate between 1938-1972 for the 362 municipalities that confirmed a plan of debt adjustment during that period was 64.7% on \$217,230,541 aggregate admitted debt.
- 1954-1972 period. Chapter 9 recovery rate between 1954-1972 for the 18 municipalities that confirmed a plan of debt adjustment during that period was 73.9% for aggregated debt per filing of \$13,227,624.

## IV. The Historic Risk of Financial Distress and Bankruptcy of Issuers in the Municipal Market

---

2. Recent default recovery rates. Recent rating agency default studies have continued to confirm the low default rate for municipal bonds. For example, in Moody's *U.S. Municipal Defaults and Recovery 1970-2014*, the municipal bond defaults for rated bonds remain extremely low, namely 1.3 defaults per year on average in the 1970-2007 period (0.01%) and 5 defaults per year in the 2008-2014 period (0 in 2014, 7 in 2013 and 5 in 2012, with an average of 5 defaults) or 0.03%. The Moody's report also notes that the ultimate recovery rate remains higher than corporate defaults with at least 64% recovery for the 1970-2014 period for municipal rated bonds versus 53% recovery for corporate senior unsecured rated bonds.

## IV. The Historic Risk of Financial Distress and Bankruptcy of Issuers in the Municipal Market

---

### 3. Recent Chapter 9 recovery rates:

- Jefferson County, Vallejo, Sierra King, Detroit ULTGOs. The recovery rate ranges vary by case, including Jefferson County, Alabama, with at least 80% of principal and interest for sewer warrants and 100% of principal for G.O. warrants, Vallejo, California, Sierra Kings Healthcare District, California (health care G.O.). Detroit (water and sewer) had a 100% recovery for special revenue debt. The Detroit Unlimited Tax General Obligation had a 100% recovery for bondholders (74% from Detroit and 26% from settlement with bond insurers).

## IV. The Historic Risk of Financial Distress and Bankruptcy of Issuers in the Municipal Market

- Detroit recovery rates.

Detroit Bankruptcy Estimated Recovery of Certain Classes of Creditors Based on Supplemental Opinion			
Type of Claim	Claim Amount	Plan Treatment	Estimated Recovery
Water and Sewer Bond (Classes 1A, 1B, 1C) Unimpaired/Nonvoting Class			100%
Secured GO Series 2010, 2010(A), 2012(A)(2), 2012 (A2-B), 2012(B), 2012(B2) (Classes 2A, 2B, 2C, 2D, 2E, 2F)			100%
Limited Tax General Obligation Bonds ("LTGO") (Class 7)	\$163.5 million	\$55 million (cash in lieu of new LTGO bonds)	41%
Unlimited Tax General Obligation Bonds (Class 8)	\$388 million Bond Insurer Bondholders	\$288 million \$388 million (26% of recovery from bond insurer)	74% 100%
Syncora Settlement on Certificates of Participation for 24.05% of Pension Bonds (COPS) (Class 9)	\$354 million	\$23.5 million New B Notes \$21.3 million New C Notes	13%
FGIC Settlement Certificates of Participation for 75.94% of Pension Bonds (COPS) (Class 9)	\$1.119 million	\$74.2 million New B Notes \$67.2 million New C Notes	13%

## IV. The Historic Risk of Financial Distress and Bankruptcy of Issuers in the Municipal Market

- How have general obligation bonds been treated in historical municipal distress and recent Chapter 9 cases?

Bankruptcy	Treatment
New York City	The G.O. Bonds were refinanced and paid-in-full by Municipal Assistance Corp. after two-year moratorium declared unconstitutional.
Orange County	All public debt with statutory liens refinanced and paid-in-full as part of the plan of debt adjustment.
Sierra King Health Care District	The unlimited ad valorem tax G.O. Bonds were paid in full and recognized as having a statutory lien and being secured by special revenues.
Jefferson County	G.O. Warrants were basically paid in full and no objection by Holders.
Detroit	See above chart on UTGOs and LTGOs. Plan of Adjustment of The Limited Tax General Obligation Bonds (LTGOs) had a 41% recovery and the Unlimited Tax General Obligation Bonds (UTGOs) had a 74%/100% with unsecured recovery, but Distributable State Aid G.O.s treated as fully secured and unimpaired with 100% recovery.



## IV. The Historic Risk of Financial Distress and Bankruptcy of Issuers in the Municipal Market

---

- Puerto Rico's approved and proposed settlement:
  - Approved settlement: There are two settlements of major public debt that have been approved namely: (1) the GDB debt of \$4.1 billion with a 55¢ on the dollar recovery and the COFINA settlement of \$17.8 billion of debt and private loans with a 93% recovery for senior and 53.5% recovery for subordinated for a blended recovery of 68%. Accordingly of public debt there is 29% of the \$73.8 billion public debt and private loans with court approved settlements.

## IV. The Historic Risk of Financial Distress and Bankruptcy of Issuers in the Municipal Market

- Puerto Rico's proposed settlements to creditors:
  - \$35 billion of claims: The \$35 billion of G.O. bond debt, Public Building Authority obligations and other debt presently supported by \$3 billion of public bond debt. The G.O. bond debt has a proposed settlement for the vintage G.O.s (pre-2012) of \$6.9 billion with a 64% recovery: the 2012 G.O.s of \$2.7 billion with a 45% recovery or litigate: the 2014 G.O.s of \$3.6 billion with a 35% recovery or litigate. The Public Building Authority obligations that the FOMB and Commonwealth are now calling debt consists of vintage PBA (pre-2012) of \$3.9 billion with a 73% recovery and the 2012 PBA of \$0.7 billion with a recovery of 23%. Also, there is other unsecured debt (non-G.O. and non-PBA unsecured creditors) of \$16 billion with a recovery of 9%. When you add the \$35 billion of proposed settlements to the \$21.6 billion of approved settlements for public debt and private loans there are about \$56.6 billion of proposed and approved settlements. Virtually all of the \$51.461 of bond and private loans contained in the fiscal plan is covered by approved proposed settlements not county ERS pension liabilities.

## IV. The Historic Risk of Financial Distress and Bankruptcy of Issuers in the Municipal Market

---

- Proposed employees' retirement systems settlement: There is also a proposed settlement of the ERS pension liabilities of about \$50 billion that proposes an 8.5% cut in pension benefits over \$1,200 a month and that affects about 39% of the retirees. This settlement proposal is supported by the Official Committee of Retired Employees.

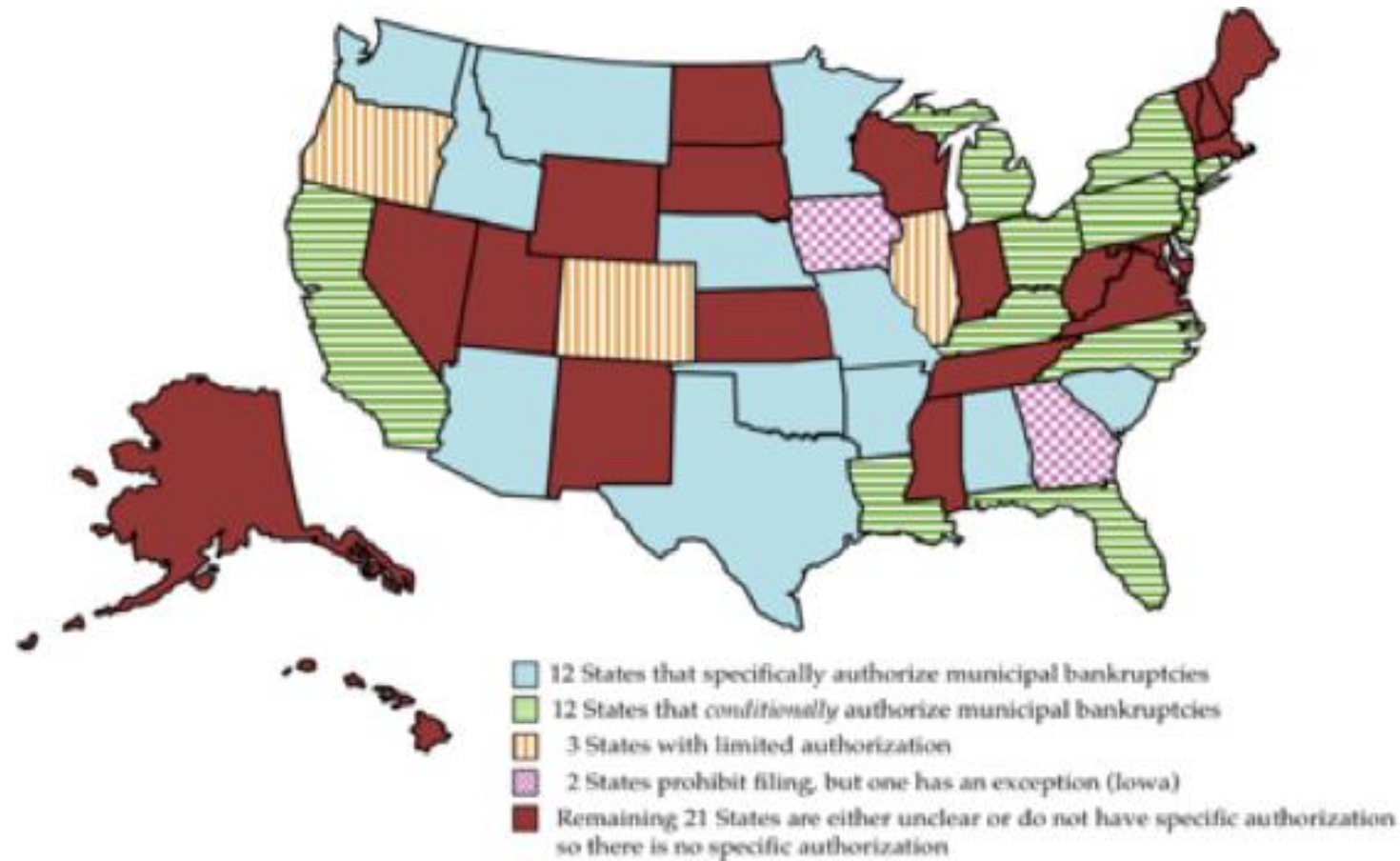
# V. Whether the Municipality Can File for Chapter 9 Bankruptcy?

- A. No Chapter 9 for states: States cannot file a Chapter 9 bankruptcy because they are co-sovereigns with the Federal Government under the U.S. Constitution (10<sup>th</sup> Amendment). States have the right as sovereigns to permit their respective sub-sovereigns (municipalities) to file.
- B. Who can be a Chapter 9 debtor?: Not every municipality can be a debtor in Chapter 9. Only municipalities in states that specifically authorize their municipalities to file can use Chapter 9. States as co-sovereigns of the federal government cannot use Chapter 9 or any federal bankruptcy forum. To be a debtor in a Chapter 9, an entity must be:
  - 1. An entity that is a municipality.

# V. Whether the Municipality Can File for Chapter 9 Bankruptcy?

2. Specifically authorized under state law to be a Debtor. Twelve states have statutory provisions in which the state specifically authorizes filing (AL, AZ, AR, ID, MN, MO, MT, NE, OK, SC, TX, WA), another twelve states authorize a filing conditioned on a further act of the state, an elected official or state entity (CA, CT, FL, KY, LA, MI, NJ, NC, NY, OH, PA, RI). Three states (CO, OR and IL) grant limited authorization, two states prohibit filing (GA) but one of them (IA) has an exception to the prohibition. The remaining 21 are either unclear or do not have specific authorization.
3. Insolvent (unable to pay its debt as they mature).
4. Willing to effectuate a plan.
5. Either has obtained the agreement of creditors holding majority amount of the claim of each class that the municipality intends to impair or has attempted to negotiate in good faith, but was unable to do so or it was impractical to negotiate with creditors or a creditor is attempting to obtain a preference.

# V. Whether the Municipality Can File for Chapter 9 Bankruptcy?



# V. Whether the Municipality Can File for Chapter 9 Bankruptcy?

The following are statutory provisions in which states have authorized Chapter 9 filings for certain governmental entities.

## 12 States that specifically authorize municipal bankruptcies:

Ala. Code 1975 § 11-81-3 (For Bonds Not Warrants)  
Ariz. Rev. Stat. Ann. § 35-603  
Ark. Code Ann. § 14-74-103  
Idaho Code Ann § 67-3903  
Minn. Stat. Ann. § 471.831  
Mo. Ann. Stat. § 427.100  
Mont. Code Ann. § 7-7-132  
Neb. Rev. St. § 13-402  
Okla. Stat. Ann. tit. 62 §§ 281, 283  
S.C. Code Ann. § 6-1-10  
Tex. Loc. Gov't Code § 140.001  
Wash. Rev. Code § 39.64.040

The 21 Remaining States are either unclear or do not have specific authorization. AK, DE, HI, IN, KS, ME, MD, MA, MS, NE, NH, NM, ND, SD, TN, UT, VA, VT, WV, WI, WY.

## 12 States that conditionally authorize municipal bankruptcies:

Cal. Gov't Code § 53760  
Conn. Gen. Stat. Ann. § 7-566  
Fla. Stat. Ann. § 218.01 and § 218.503  
Ky. Rev. Stat Ann. § 66.400  
La. Rev. Stat. Ann. § 39-619  
Mich. Comp. Laws § 141.1222  
N.J. Stat. Ann. § 52:27-40  
N.C. Gen. Stat. Ann. § 23-48  
N.Y. Local Finance Law § 85.80  
Ohio Rev. Code Ann. § 133.36  
53 Pa. Cons. Stat. Ann. § 11701.261  
R.I. Gen. Laws § 45-9-7

## 3 States with limited authorization

- Colorado has enacted legislation specifically authorizing its beleaguered special taxing districts to file a petition under Chapter 9. Section 32-1-1403 of the Colorado revised statutes states that "any insolvent taxing district is hereby authorized to file a petition authorized by federal bankruptcy law and to take any and all action necessary or proper to carry out the plan filed with said petition..." (CRS § 37-32-102 (Drainage & Irrigation District))
- Oregon permits Irrigation and Drainage Districts to file (Or. Rev. Stat. § 548.705)
- Illinois – specific authorization solely for the Illinois Power Agency (20 Ill Comp. Stat. Ann. 3855/1-20(b)(15)). The Local Government Financing and Supervision Act permits that commission to recommend that the Legislature authorize a filing but it is not specific authorization (20 Ill. Comp. Stat. Ann. 320/9(b)(4))

## 2 States prohibit filing but one has an Exception

- Iowa generally prohibits filing Chapter 9 (Ia. Code Ann. § 76.16) but allows filing for insolvency caused by debt involuntarily incurred not covered by insurance proceeds (Ia. Code Ann. § 76.16A)
- Georgia prohibits the filing of Chapter 9 Bankruptcy (Ga. Code Ann. § 36-80-5)

# V. Whether the Municipality Can File for Chapter 9 Bankruptcy?

---

- C. Ability to be paid if the issuer is not authorized to file Chapter 9: Where there is no authorization to file then the questions are what remedies upon default are available and are they regularly enforced by the courts of the states and what state aid and assistance are available to address the problem. These questions will be answered in the following discussion.



# VI. What Is the Source of Payment?

- A. Determining the type of obligation and the source of payment: Is the general obligation debt a "naked" full faith and credit promise or does it have a pledge of special revenues or statutory lien pledging and dedicating a specific and adequate tax revenue source of payment. Does the revenue bond have a dedicated revenue payment source that is sufficient to make all payments with an appropriate rate covenant that is deemed to be special revenues. (As noted above, Alexander Hamilton in the 1790s said the secret of making public credit "immortal" is that whenever public debt is increased, it ought to be accompanied by a sufficient tax increase dedicated to its payment. Syrett, The Papers of Alexander Hamilton, Vol. 6, p. 106 and Vol. 18, p. 103.)

# VI. What Is the Source of Payment?

## B. Summary of types of bonds and treatment in Chapter 9:

Summary of Basic Treatment of Bonds and Notes in Chapter 9	
Type of Bonds/Notes	Bankruptcy Effects
General Obligation Bonds Without a Specific Pledge	<p>Post-petition, a court may treat general obligation bonds as unsecured debt which do not have a statutory lien or constitutionally mandated payment of dedicated revenues or a pledge of revenues that classifies as special revenues and the court may order a restructuring of the bonds. Payment on such bonds during the bankruptcy proceeding likely will cease.</p> <p>Pre-petition, unlimited general obligation bonds are backed by the unlimited taxing power of the municipality (its "full faith and credit") and are historically subject to conditions such as voter authorization, limitations on particular purposes, or debt limitation to a percentage of assessed valuation on the power of municipal entities to incur such debts.</p>

# VI. What Is the Source of Payment?

Summary of Basic Treatment of Bonds and Notes in Chapter 9	
Type of Bonds/Notes	Bankruptcy Effects
General Obligation Bonds plus Pledged Revenues	Assuming that the general obligation pledge is an actual pledge of specific revenue and to the extent that it may be classified as a statutory lien or constitutionally mandated payment of dedicated revenues or special revenues, this secured issuance will be respected to the degree it is consistent and authorized under state law. A contractual pledge of revenues that is not a statutory lien or constitutionally mandated payment of dedicated revenues or special revenues may be attacked as not being a valid continuing Post-Petition Lien under § 552 of the Bankruptcy Code. However, state law mandated payments of revenues whereby the force and effect of language of the state statute or constitutional provision payments related to dedicated revenues, set-aides, priorities, or appropriateness are mandated to be made ("State Law Mandated Payments") should be paid post petition as collected without delay. This would be consistent with §§ 903 and 904 of the Bankruptcy Code because the <i>Ashton</i> and <i>Bekins</i> cases the prohibition that the court not interfere with the power of a State to control a municipality in exercise of political or governmental powers the government affairs or revenues of the municipality.

# VI. What Is the Source of Payment?

Summary of Basic Treatment of Bonds and Notes in Chapter 9	
Type of Bonds/Notes	Bankruptcy Effects
Special Revenue Bonds	<p>A pledge of special revenues will survive a bankruptcy filing. Pre-petition, a special revenue bond is an obligation to repay solely and only from specific revenues of a municipal enterprise (net of operations and maintenance costs, if applicable) or dedicated funds or tax revenues that are pledged to bondholders. No stay during the Chapter 9 proceeding in payment of such special revenues to pay the debt it is pledged to pursuant to the terms of the documents. (§ 922(d)). The contemplated remedy for default often focuses on a covenant to charge rates sufficient to amortize the debt and, if necessary, the appointment of a receiver. Defaulted bondholders are expected to seek mandamus in court to require the municipal borrower to raise its rates or, if necessary, the appointment of a receiver to enforce the rate covenant and prudent operations of the municipal enterprise. To enforce such remedies after the filing of a Chapter 9 would require the lifting of the automatic stay.</p>

# VI. What Is the Source of Payment?

Summary of Basic Treatment of Bonds and Notes in Chapter 9	
Type of Bonds/Notes	Bankruptcy Effects
Revenues Subject to Statutory Lien	Assuming the pledge is authorized under state law through a statutory lien, the bankruptcy court should respect that statutory lien. Thus, as long as the revenues are subject to a statutory lien, payments to the bondholders should be protected post-petition and, based on Sections 903 and 904 of the Bankruptcy Code and the <i>Ashton</i> and <i>Bekins</i> cases, should be paid to the bondholder as mandated by the statute.

# VI. What Is the Source of Payment?

## C. Summary of Chapter 9 priorities:

Summary of Chapter 9 Priorities		
Type of Claim		Explanation
1.	Obligations secured by a statutory lien to the extent of the pledged revenue collected. <sup>ab</sup>	Debt (Bonds, Warranties, Notes, Trans, Rans) issued pursuant to statute that itself imposes a pledge. (There should not be any delay in payments due to automatic stay since the Bankruptcy Court and municipality have no authority to do otherwise due to the mandate of state law to only use or expend revenues or proceeds for the designated purpose under § 903 of the Federal Bankruptcy Code and the municipality cannot act or consent differently since it is unable to do so under state law that controls under § 904 of the Federal Bankruptcy Code.)

- a Chapter 9 incorporates § 506(c) of the Bankruptcy Code which imposes a surcharge for preserving or disposing of collateral. Because a municipality cannot mortgage city hall or the police headquarters, municipal securities tend to be secured by a pledge of a revenue stream. Hence, it is seldom a surcharge would be imposed. *But see* numbers 3 and 4.
- b Chapter 9 incorporates § 364(d) of the Bankruptcy Code, which permits a debtor to obtain post-petition credit secured by a senior or equal lien on property of the estate that is subject to a lien if the prior lien holder is adequately protected. However, if state law mandates the use of the pledge revenues solely or first to pay the statutory lien or special revenue debt that mandate of state law cannot be violated and no priming lien or other use of revenues can be authorized. State Law Mandated Payments where the force and effect of the state statutory or constitutional language mandate the municipality make the payment of dedicated revenues to the specified debt pursuant to pledged revenues, set-asides, priorities as to the use of revenues or required appropriation shall be treated similar to a statutory lien as set forth in subsection F below and Sections 903 and 904 of the Bankruptcy Code and the U.S. Supreme Court rulings in the *Ashton* and *Bekins* cases.

# VI. What Is the Source of Payment?

Summary of Chapter 9 Priorities		
Type of Claim		Explanation
2.	<p>Obligations secured by special revenues (subject to necessary operating expenses of such project or system if applicable) to the extent of the pledged revenue collected.<sup>ab</sup> These obligations are often non-recourse and, in the event of default, the bondholders have no claim against non-pledged assets.</p> <p>(Reaffirmed in Jefferson County Court Ruling and the ultimate treatment of Water and Sewer Revenue Bonds in Detroit.)</p>	<p>Special revenue bonds secured by any of the following:</p> <p>(A) receipts derived from the ownership, operation, or disposition of projects or systems of the debtor that are primarily used or intended to be used primarily to provide transportation, utility, or other services, including the proceeds of borrowings to finance the projects or systems; (B) special excise taxes imposed on particular activities or transactions; (C) incremental tax receipts from the benefited area in the case of tax-increment financing; (D) other revenues or receipts derived from particular functions of the debtor, whether or not the debtor has other functions; or (E) taxes specially levied to finance one or more projects or systems, excluding receipts from general property, sales, or income taxes (other than tax-increment financing) levied to finance the general purposes of the debtor.<sup>c</sup></p> <p>There should be no delay in payment since automatic stay is lifted under Section 922(d).</p> <p>If the state statute also creates a statutory lien or mandate that the pledged tax revenues can only be used for payment of the debt obligations and for no other purposes before payment in full of the obligation then no reduction for necessary operating expenses – §§ 903, 904 and 928 of the Federal Bankruptcy Code.</p>

<sup>c</sup> A pledge of revenues that is not a statutory lien or special revenue pledge may be attacked as not being a valid continuing post-petition lien under § 552 of the Bankruptcy Code.

# VI. What Is the Source of Payment?

Summary of Chapter 9 Priorities		
Type of Claim		Explanation
3.	Secured lien based on bond resolution or contractual provisions that does not meet test of statutory lien or special revenues to the extent perfected prepetition, subject to the value of prepetition property or proceeds thereof. <sup>c</sup>	Under language of Sections 552 and 928, liens on such collateral would not continue postpetition. After giving value to the prepetition lien on property or proceeds, there is an unsecured claim to the extent there is recourse to the municipality or Debtor. You may expect the creditor to argue that pursuant to Section 904, the Court cannot interfere with the property or revenues of the Debtor (without the Debtor's consent consistent with state law), and that includes the grant of security to such secured creditor.
4.	Obligations secured by a municipal facility lease financing.	Under Section 929 of the Bankruptcy Code, even if the transaction is styled as a municipal lease, a financing lease will be treated as long-term debt and secured to the extent of the value of the facility.



# VI. What Is the Source of Payment?

Summary of Chapter 9 Priorities		
Type of Claim		Explanation
5.	Administrative expenses (which would include expenses incurred in connection with the Chapter 9 case itself). <sup>d</sup> Chapter 9 incorporates Section 507(a)(2) which, by its terms, provides a priority for administrative expenses allowed under Section 503(b). These would include the expenses of a committee or indenture trustee making a substantial contribution in a Chapter 9 case. <sup>d</sup> These expenses strictly relate to the costs of the bankruptcy. Because the bankruptcy court cannot interfere with the government and affairs of the municipality, general operating expenses of the municipality after filing of the Chapter 9 are not within the control of the court (unless the municipality consents and is not otherwise prohibited under state law from interfering with the payment), are not discharged and will remain liabilities of the municipality after the confirmation of a plan or dismissal of the case.	Pursuant to Section 943, all amounts must be disclosed and be reasonable for a plan of adjustment to be confirmed.

<sup>d</sup> These expenses strictly relate to the costs of the bankruptcy. Because the bankruptcy court cannot interfere with the government and affairs of the municipality, general operating expenses of the municipality after filing of the Chapter 9 are not within the control of the court (unless the municipality consents and is not otherwise prohibited under state law from interfering with the payment), are not discharged and will remain liabilities of the municipality after the confirmation of a plan or dismissal of the case.

# VI. What Is the Source of Payment?

Summary of Chapter 9 Priorities		
Type of Claim		Explanation
6.	Unsecured debt includes:	
	A. Senior unsecured claims with benefit of subordination paid to the extent of available funds (without any obligation to raise taxes) which include any of B, C, D, or E below.	
	B. General Obligation Bonds.	With a general pledge of "full faith and credit" of the issuing municipality (unlimited or limited) without a dedication of special revenues or a statutory lien. Post petition, a court may treat general obligation bonds without a statutory lien or special revenues pledge as unsecured debt and permit an adjustment or restructuring of the bonds. Payment on the bonds during the bankruptcy proceeding likely will cease. <sup>e</sup>
	C. Trade.	Vendors, suppliers, contracting parties for goods or services. Payment will likely cease for prepetition goods or services. <sup>f</sup>

<sup>e</sup> However, if state law mandates specific appropriation, set aside or priority of payment of revenue collected the failure to honor state law may be an obstacle to confirming a plan of debt adjustment since the plan, court and municipality cannot go forward. See § 903 of Federal Bankruptcy Code.

<sup>f</sup> Section 503(b)(9) provides for a priority claim to be paid on confirmation of a plan for the value of goods provided prepetition within 20 days of the petition date.

# VI. What Is the Source of Payment?

Summary of Chapter 9 Priorities		
Type of Claim		Explanation
	D. Obligations for Accrued but Unpaid Prepetition Wages and Pensions and other Employee Benefits.	These do not enjoy any priority, unlike in a Chapter 11. <sup>g</sup>
	E. Unsecured portion of secured indebtedness.	
	F. Subordinated Unsecured Claims.	Any debt subordinated by statute or by contract to other debt would be appropriately subordinated and paid only to the extent senior claims are paid in full. Senior debt would receive combined senior and subordinate <i>pro rata</i> distribution (the distribution attributable to the aggregate senior and subordinated unsecured claim) until the senior is paid in full.

<sup>g</sup> Chapter 9 does not incorporate § 1113 of the Bankruptcy Code, which imposes special provisions for the rejection of collective bargaining agreements (making the standard less restrictive, *i.e.*, "impairs ability to rehabilitate") or § 507(a)(4) and (5), which give a priority (before payment of unsecured claims) to wages, salaries, commissions, vacation, severance, sick leave or contribution to pension plans of currently \$12,850 per employee.

## VII. Is There a Lack of Diversification of Tax Sources and Limits on Taxes That Could Realistically Be Triggered

---

Are sources of tax revenues too limited or are there tax limits and debt limits close to being triggered that may prevent the raising of taxes to pay the obligation.

A. Diversification of tax sources to prevent over-concentration of source of funding:

1. Since the Depression of the 1930's, state and local governments have diversified the source of tax revenues to reduce reliance on property taxes and to spread the burdens and reduce the risk of concentration – that diversity of tax sources has made a real difference in the eleven economic downturns since 1949 especially in 2008.

## VII. Is There a Lack of Diversification of Tax Sources and Limits on Taxes That Could Realistically Be Triggered

### General State and Local Governments Revenues 1922-2008: Totals and Percentage Distribution

	1922	1927	1932	1936	1940	1968	2008
Amount of Gen. Rev. (billions of dollars)	4.8	7.3	7.3	8.4	9.6	101.3	2425.8
Percent Distribution							
Property Tax	69.5	65.1	61.7	48.8	46.1	27.4	16.7
Sales Tax	3.2	6.5	10.3	17.7	20.6	22.6	18.5
Income Tax	2.1	2.2	2.1	3.2	4.0	9.7	14.8
Other Tax	9.2	10.0	10.6	10.2	10.6	7.0	4.5
Misc. Rev.	13.7	14.7	12.0	8.9	8.9	16.3	25.7
Federal Aid	<u>2.3</u>	<u>1.6</u>	<u>3.2</u>	<u>11.3</u>	<u>9.8</u>	<u>17.0</u>	<u>19.8</u>
<b>TOTAL</b>	100.0	100.0	100.0	100.0	100.0	100.0	100.0

- Property, income and sales taxes made up over 70% of state and local governments revenues in 1922-1940 but only 50% of state and local governments revenue by 2008. More diverse and varied tax base in 2008 with more federal assistance.
- Property taxes which made up over 60% of the revenues of state and local governments between 1922-1932 was only 16.7% of revenue by 2008 with increases in sale, income other, miscellaneous and federal aid making up the difference.

## VII. Is There a Lack of Diversification of Tax Sources and Limits on Taxes That Could Realistically Be Triggered

**But will this diversity of tax sources and strength of tax revenues and collections be true for the foreseeable future?**

Not necessarily!

The digital, shared economy and artificial intelligence (automation) revolution has put the strength of diverse tax revenue sources into question:

- (a) Online sales. Increased online sales will threaten traditional sale tax receipts and, as online sales increase and the sale tax revenues are not collected or not collected in the jurisdiction the purchaser resides, there will be a loss of sale tax revenue from the traditional sale tax government tax collector. Amazon Distribution Centers are not located in major metropolitan areas where the bulk of the Amazon purchasers reside. The U.S. Government Accountability Office estimates the loss of sales tax revenues due to online sales to be \$8 billion to \$13 billion in 2017 while the National Conference of State Legislatures and International Council of Shopping Centers estimated the sales tax loss to the states in 2015 to be \$26 billion.

## VII. Is There a Lack of Diversification of Tax Sources and Limits on Taxes That Could Realistically Be Triggered

---

- (b) Autonomous electric cars by 2026. California Department of Transportation predicts major highways in California may well be, by 2026, restricted to electric level IV autonomous cars. What will happen to gas tax revenues and related bond issues, or employees in manufacturing of combustion engines, vehicles and related fields, e.g., car repairs or sales? What will be the effect of the probable reduction of employed workers in related fields of oil and gas, refineries, auto and auto parts, manufacturing for combustion engines, vehicles and machines, auto repairs, etc., which is estimated to decrease 20-30% each year after 2025, and the resulting loss of those workers' income tax and sale tax revenues and increase in unemployment benefits?

## VII. Is There a Lack of Diversification of Tax Sources and Limits on Taxes That Could Realistically Be Triggered

- (c) Shared economy. With autonomous electric cars used by Uber and Lyft, and the reduction or virtual elimination of private ownership of vehicles, what is the result in lost parking lot tax revenues (since cars do not park all day due to constant use and little individual ownership), loss of employment for parking lot servicing employees and related loss of income tax revenues as well as reduced number of vehicles needed due to the "more efficient use of vehicles by reduced individual ownership"? Also, various equipment used occasionally in home ownership will not need to be purchased individually but will be shared on a collective "rent" or "ownership" basis. Possible significant decrease of taxi fees, traffic violation fines, parking taxes, vehicle registration fees and toll road collections, etc. In addition, Turo allows individual car owners to rent their cars to the public as part of the shared economy.



## VII. Is There a Lack of Diversification of Tax Sources and Limits on Taxes That Could Realistically Be Triggered

- (d) Expanded use of automation and artificial intelligence. As automation continues to evolve and workers are replaced by robots, what should be the replacement tax on robots, the cost of out-of-work workers, the lost income and lost sales tax revenues from personal consumption of goods and services? Should there be a robot replacement tax to capture all the lost revenues?
- (e) The increased use of Airbnb. With the Airbnb phenomenon, there will be loss of local hotel and convention taxes, loss of jobs in the hotel industry and possible lack of safety standards for vacation and visitor guest rooms. Most major cities, as well as smaller ones, have made budgets balance and needed capital improvement projects funded by a hotel and convention tax. Those taxes will be difficult to collect, enforce and levy on individual home and apartment owners in this yet to be regulated cottage industry.

## VII. Is There a Lack of Diversification of Tax Sources and Limits on Taxes That Could Realistically Be Triggered

---

### 2. Use of debt limitation and tax limitation:

- (a) Virtually all states impose some sort of limitation on the amount of debt or tax limitations or both. (See Appendix I taken from the recently released Second Edition of "Municipalities in Distress? How States and Investors Deal with Local government Financial Emergencies").
- (b) Municipal debt limits range from a percentage of a valuation of assessed property to a monetary amount. Will these limits be appropriate and effective given the effects of the digital, shared economy and artificial intelligence revolution?
- (c) States handle debt for essential services differently than for non-essential.
- (d) There have been recent attempts in some states to tighten local debt limits while others strengthen protections.

## VII. Is There a Lack of Diversification of Tax Sources and Limits on Taxes That Could Realistically Be Triggered

- (e) Generally, revenue bonds paid from the revenues of a municipal enterprise (water, sewer, bridge, tollway, electric system) are exempt from debt limits. So also are tax increment financing and appropriation bonds.
  - (f) With unresolved obligation for public workers' unfunded pension and health care costs, as well as growing deferred needed infrastructure improvement costs, at the same time there are decreasing tax revenues compared to traditional revenue source, statutory and constitutional debt and tax limits may need to be increased. What are the good as gold tax revenues that will remain and what new ones need to be developed to avoid increasing tax and debt limits.
3. Refunding bonds are permitted in all states. (See Appendix I for further breakdown.) But, if the sources of tax revenues are drastically changed by the effects of digital, shared economy and artificial intelligence implementation, what will be the new assured tax revenues of the future?

## VII. Is There a Lack of Diversification of Tax Sources and Limits on Taxes That Could Realistically Be Triggered

B. The need to reexamine the future viability of current tax revenue sources and consider new policies and sources for taxes to survive the digital, shared economy and artificial intelligence revolution:

1. Threat to current financings. If there will be autonomous cars, use of shared economy rooms in apartments and homes and not continued use of hotels, then there will be less use of hotels, cars, parking garages, etc. and less tax revenue from them. The future of current financings that have 10-20 years to maturity relying on such taxes on hotel, parking, gas, etc., as repayment sources will be a challenged.

The viability and sufficiency of tax sources and general tax policy will need to be examined and refined to meet the challenges of the digital/automation/shared new reality.

## VII. Is There a Lack of Diversification of Tax Sources and Limits on Taxes That Could Realistically Be Triggered

2. Is it too late to start or too early? An analysis of the long-term sufficiency of current source of tax revenues can never begin too early or start too late. Based on the lesson of the 1930's Depression, if the tax revenue source is the subject of a major change, those financings and funding targets need to be correspondingly modified to deal with the evolving flow of possible tax revenues.

Whether there will be an automation tax or robot tax to cover lost tax revenues of displaced unemployed workers or a value-added tax for increased manufacturing productivity due to automation or other new tax formulae or methods of taxing will be the subject of spirited debate and experiment.

## VII. Is There a Lack of Diversification of Tax Sources and Limits on Taxes That Could Realistically Be Triggered

3. What are some of the possible new tax sources states and local government may utilize in the future?
  - Graduated state income tax (*i.e.*, 34 states granted income tax and 7 states have a flat tax income).
  - City income tax (like New York City, Philadelphia, Indianapolis, Louisville, Newark, Detroit, etc.).
  - City commuter tax.
  - Expanding state and city sales tax.
  - State or city financial transaction tax.
  - Graduated real estate transfer tax.
  - State recreational marijuana tax with city sharing.
  - New gaming taxes including authorizing land-based casino.
  - Expanded property tax.

## VII. Is There a Lack of Diversification of Tax Sources and Limits on Taxes That Could Realistically Be Triggered

---

- City employer expense tax (the old head tax).
- City congestion tax.
- State reduction or elimination of income tax deduction such as retirement income with city sharing.
- Expanded service tax targeting non-health and food-related high-end service providers.
- Privatization revenues.
- Automation tax (payable over useful life of the equipment) on new automation equipment that causes the loss of employment due to use of the equipment and tax based on cost to retained unemployed workers and loss of tax revenue due to loss of taxable income from unemployed workers.

## VIII. Is Effective State Oversight and Assistance Available to Prevent Defaults or Aid a Financially Troubled Municipality?

Does the state provide by statute or practice the ability to monitor and oversee a financially challenged municipality, provide financial guidance and support to bridge the economic downturn and avoid litigation meltdown and Chapter 9.

A. Growing and increased use of state oversight, supervision and assistance for emergencies of local governments:

1. At least twenty-eight states, the District of Columbia and Puerto Rico have implemented some form of municipal debt supervision or restructuring mechanism to aid municipalities:
  - (a) These range from Debt Advisory Commissions (e.g., California) and Technical Assistance Programs (Florida) which provide guidance for and keep records of issuance of municipal debt to the layered approach of Rhode Island and Michigan of oversight commission and fiscal manager or receiver. (See Appendix for further details.)



## **VIII. Is Effective State Oversight and Assistance Available to Prevent Defaults or Aid a Financially Troubled Municipality?**

---

- (b) There has been a recent trend of increased legislation providing oversight, supervision, assistance and even financial aid to distressed municipalities:
  - Municipal Accountability Review Board (MARB) in Connecticut (2017).
  - Revision to Act 47 (31 designated since 1988, 14 rescinded and 17 pending) in Pennsylvania (2014).
  - Michigan legislation requires municipalities to report on the municipal pension fund health and established a municipal stability board to review municipal financing and develop a recovery plan for pension programs, but not emergency manager or financial control by state for municipal pension plans that are in distress (2017).
- (c) Examples of state oversight, supervision and assistance for fiscal emergencies of local government will follow.

## VIII. Is Effective State Oversight and Assistance Available to Prevent Defaults or Aid a Financially Troubled Municipality?

	STATE	INTERVENTION PROVISION
1.	Arizona	School District Receivership
2.	California	Debt and Investment Advisory Commission
3.	Connecticut	Ad Hoc State Intervention/Municipal Accountability Review Board (MARB)
4.	District of Columbia	Financial Responsibility and Management Assistance Authority
5.	Florida	Bond Financial Emergencies Act; Division of Bond Finance and Local Government Financial Technical Assistance Program
6.	Georgia	Government Monitoring
7.	Idaho	Debt Readjustment Plans
8.	Illinois	Financially Distressed City Law; Financial Planning and Supervision
9.	Indiana	Distressed Political Subdivision Protections and Township Assistance
10.	Kentucky	County Restructuring Provisions

## VIII. Is Effective State Oversight and Assistance Available to Prevent Defaults or Aid a Financially Troubled Municipality?

	STATE	INTERVENTION PROVISION
11.	Louisiana	Appointment of a Fiscal Administrator
12.	Maine	Board of Emergency Municipal Finance
13.	Massachusetts	Ad Hoc State Intervention and State Bond Payment Intervention
14.	Michigan	Local Financial Stability and Choice Act
15.	Minnesota	Back-up Payment Procedures for Municipalities and School Districts
16.	Nevada	Local Government Financial Assistance and Audit Enforcement Act
17.	New Hampshire	Emergency Financial Assistance
18.	New Jersey	Local Government Supervision Act; Municipal Rehabilitation and Economic Recovery Act of 2002; Special Municipal Aid Act
19.	New York	Emergency Financial Control Board; Municipal Assistance Corporation; New York Financial Control Board; State Comptroller's Fiscal Stress Monitoring System

## VIII. Is Effective State Oversight and Assistance Available to Prevent Defaults or Aid a Financially Troubled Municipality?

	STATE	INTERVENTION PROVISION
20.	New Mexico	Financial Auditing and Emergency Loans
21.	North Carolina	Local Government Finance Act
22.	Ohio	State Auditor's Fiscal Caution and Fiscal Watch; Fiscal Emergencies and Financial Planning and Supervision Commission
23.	Oregon	County Technical Assistance Program; Municipal Debt Advisory Commission
24.	Pennsylvania	Financially Distressed Municipalities Act; Intergovernmental Cooperation Act; Municipal Receiver
25.	Puerto Rico	Puerto Rico Oversight, Management and Economic Act
26.	Rhode Island	Fiscal Overseer; Municipal Receiver; Budget Commission
27.	Tennessee	Emergency Financial Aid to Local Governments; Financially Distressed Municipality Procedures
28.	Texas	Municipal Receivership

## VIII. Is Effective State Oversight and Assistance Available to Prevent Defaults or Aid a Financially Troubled Municipality?

	STATE	INTERVENTION PROVISION
29.	Virginia	Bond Payment Guarantee Provisions
30.	Wisconsin	Deficiency Protection for Public Improvement Bonds

(For more detail on state by state overview of rights and remedies provided by states to investors relating to bond debt and state oversight supervision of financial emergencies and authorization to file Chapter 9 see Appendix I herein which is taken from Municipalities in Distress? 50 State Survey in the 2<sup>nd</sup> Edition.)

## **VIII. Is Effective State Oversight and Assistance Available to Prevent Defaults or Aid a Financially Troubled Municipality?**

---

### **B. States recognize the use of a municipal receiver:**

1. The Rhode Island experience and the City of Central Falls:
  - (a) Overseers.
  - (b) Budget Commission.
  - (c) Receiver.
  - (d) Chapter 9.
2. Texas' use of judicially appointed receiver vs. financial control board, emergency financial managers, coordination overseers and refinance.

## VIII. Is Effective State Oversight and Assistance Available to Prevent Defaults or Aid a Financially Troubled Municipality?

### C. Financial control boards and active supervision examples:

1. The Rhode Island experience and the City of Central Falls.
2. The New York experience – Financial Control Board.
3. The Pennsylvania experience – Act 47.
4. The Michigan and Indiana experience – Emergency Managers.
5. The Massachusetts *Ad Hoc* experience.
6. The California experience – Neutral Evaluator.
7. The North Carolina – Local Government Commission – oversight and approval from the cradle if debt issued to annual financial reports.
8. Puerto Rico – Puerto Rico Oversight, Management and Economic Stability Act.
9. MARB – For the oversight and state assistance to the City of Hartford.

## **VIII. Is Effective State Oversight and Assistance Available to Prevent Defaults or Aid a Financially Troubled Municipality?**

- D. Development of a Municipal Protection Commission as a quasi judicial entity to determine what costs are sustainable and affordable and which are not, including labor costs and benefits and whether taxes should be raised or costs reduced.
- E. The structure for oversight and emergency financing:
  - 1. Grants from federal, state and regional governmental bodies.
  - 2. Loans from federal, state and regional governmental bodies.
  - 3. State intercepts of tax revenue.
  - 4. Involvement in local government budget process.
  - 5. Required financial performance and targeted levels of essential governmental services.
  - 6. State legislative assistance in tax revenue and powers.
  - 7. Back-up by moral obligations of the state.



## **VIII. Is Effective State Oversight and Assistance Available to Prevent Defaults or Aid a Financially Troubled Municipality?**

---

8. Considerations regarding the appointment of authority members.
9. Acceleration of loans and obligations if performance triggers are violated
10. Dealing with the press.
11. What powers are essential for state oversight and assistance.
12. Exploration of transfer of certain governmental services (and related costs) to other governmental bodies.
13. Consolidation of regional essential governmental services.
14. Power to authorize Chapter 9 if needed or bridge financing or refinancing of troubled debt.
15. Use of intercept of state tax payable to municipality to ensure essential municipal service.
16. Private public partnerships – Lease and sale of municipal properties to provide bridge financing and cash flow relief.

## **VIII. Is Effective State Oversight and Assistance Available to Prevent Defaults or Aid a Financially Troubled Municipality?**

---

17. Vendor assistance program – Providing vendor payments through securitization financing of payables. Payment from dedicated tax revenues over time. Provide current cash flow relief from current or future vendor payments.
18. Explore consolidation on a regional basis of certain governmental services.
19. Monitor compliance with any restructuring plan to ensure compliance and prevent financial erosion.

## **VIII. Is Effective State Oversight and Assistance Available to Prevent Defaults or Aid a Financially Troubled Municipality?**

---

- F. Applicable state assistance, refinancing and restructuring mechanism should be disclosed:
  - 1. To the degree state has effective and applicable mechanism to help prevent default or provide funds or assistance to prevent default or methods of solving financial problems of municipal issuers this is information important to the investor and should be considered to be disclosed to the investor. Such information may improve the perception of the issuer's credibility in the market.

## **IX. The Need for Uniform Pension Underfunding Disclosure and Whether Such Underfunding Is Crowding Out Funding of Essential Services and Needed Infrastructure**

### **A. State and local government pension funds status:**

1. Almost 6,000 public sector retirement systems for state and local governments in the United States with \$4.3 trillion in assets, about 14.5 million current employees, 10.3 million retirees and annual aggregate benefit distributions of \$283.4 billion (U.S. Census Bureau).
2. The amount of pension underfunding for states and local governments is estimated to range between \$1 to \$3 trillion.
3. This unfunded liability for pensions can be compared to the estimated FY2016 tax revenue of \$1.6 trillion for state and local governments.

## **IX. The Need for Uniform Pension Underfunding Disclosure and Whether Such Underfunding Is Crowding Out Funding of Essential Services and Needed Infrastructure**

4. A recent national survey of 168 leading state and local government credit analysts asked "What do you think are the five most important issues/trends facing the municipal bond market right now [March 2018]?" Ninety-two percent responded, "public pension funding levels, pension obligation bonds." See PNC, U.S. Municipal Bond Market, Municipal Bond Analyst Survey 2018 (April 5, 2018), Thomas Kozik.
5. In October 2018, The Center for Retirement Research at Boston College Report noted:
  - (a) The average funded ratio between 2001-2017 demonstrates:
    - The top third funded pension funds were 110% funded on average in 2001 compared to 90% in 2017, a 20% drop.
    - The middle third pension funds were 100% funded on average in 2001 compared to 73% in 2017, a 27% drop.
    - The bottom third pension funds were 90% funded on average in 2001 compared to 55% in 2017, a 35% drop.

## **IX. The Need for Uniform Pension Underfunding Disclosure and Whether Such Underfunding Is Crowding Out Funding of Essential Services and Needed Infrastructure**

- While some may place the criticism and blame on the failure of state and local governments between 2001 and 2017 to fully fund the actuarially determined contribution that would assure at least 90% funding in 30 years or less, there were other more devastating and depressing forces that fostered substantial loss
- Between March 2000 to October 2002, the S&P 500 lost 49.1% in value and between October 2007 to March 2009, the S&P 500 lost 56.4% in value.
- Is pension underfunding caused more by the lack of adequate funding or by losses on investments given economic downturns?
- It is interesting to note that the Illinois public pension systems combined funding ratio in 2000 was about 74.7% and the unfunded liability in 2000 was \$15.569 billion and by the end of fiscal year 2018 funded ratio was about 40.1% and the unfunded liability was \$133.7 billion.

## **IX. The Need for Uniform Pension Underfunding Disclosure and Whether Such Underfunding Is Crowding Out Funding of Essential Services and Needed Infrastructure**

---

- B. Many state and local governments have no current pension fund problem or have resolved it: It should be noted that a number of states (see *e.g.*, Wisconsin, Tennessee, South Dakota, Utah, Alaska, North Dakota) and local governments (Washington D.C., Denver, Scottsdale, Indianapolis, Raleigh) have or will successfully address public pension issues without extensive prolonged disputes or litigation.

## IX. The Need for Uniform Pension Underfunding Disclosure and Whether Such Underfunding Is Crowding Out Funding of Essential Services and Needed Infrastructure

- C. The aging population and possible future economic downturn are reasons to be vigilant no matter the current conditions of the pension fund: Those over 65 years of age in the United States constitute an increasing percent of the population, namely 14.8% of the 2015 population, which is expected to grow to 20.9% by 2050. Likewise, the working years of 18-64 of age is expected to be reduced as a percent of population, namely from 62.2% in 2015 to 57.6% in 2050. This results in about 40 million more people over 65 as potential retirees.

While the USA percentage of population over 65 may be lower than many other developed countries in 2050, such as Europe at 26%, China at 24% and Japan at 33%, it is still a concern. Likewise there have been 11 economic downturns since 1949, about one every 7 to 10 years, so we now are facing the probability of an economic downturn in the next few years since the last downturn was 2008.

Economic downturns result in losses on pension fund investments and less revenues available to state and local governments to address the issues.



## IX. The Need for Uniform Pension Underfunding Disclosure and Whether Such Underfunding Is Crowding Out Funding of Essential Services and Needed Infrastructure

---

- D. Recent pension reform and litigation: Between 2010 and 2018, over 46 states have addressed pension reform. To date, since 2011, there have been over 25 major state court decisions dealing with pension reforms by state and local governments:
1. Over 80% (21 out of 25) of those decisions affirmed the pension reform, which covered reduction of benefits, including COLA, or increase of employee contributions, as necessary, and many times cited the higher public purpose of assuring funds for essential governmental services and infrastructures.
  2. Of the four states that did not approve the pension reform, two states, Oregon and Montana, cited the failure of the proponents of reform to prove a balancing of equities in favor of reform for a higher public purpose.

## IX. The Need for Uniform Pension Underfunding Disclosure and Whether Such Underfunding Is Crowding Out Funding of Essential Services and Needed Infrastructure

---

### E. Examples of recent pension reforms and pension reform litigation:

1. California: California's Pension Reform of 2012 estimated savings of between \$42 billion - \$55 billion for CalPERs and \$27.7 billion for CALSTRs.
2. Rhode Island: Rhode Island's Pension Reform and Interim Suspension of COLA, created hybrid pension plans for non-public safety employees and increased the minimum retirement age. The dispute over this reform was originally settled, but then the police union rejected the proposed settlement. Ultimately, there was a settlement of the litigation, and the reforms were implemented with some settlement adjustments. Rhode Island Supreme Court in June 2019 reaffirmed the need for pension reform in the City of Cranston case noting the severe financial crisis caused in part by unaffordable pension benefits mandated reform and reduction of benefits for the higher public purpose of funding essential services for the health, safety and welfare of its citizens.

## IX. The Need for Uniform Pension Underfunding Disclosure and Whether Such Underfunding Is Crowding Out Funding of Essential Services and Needed Infrastructure

3. COLA litigation: COLA litigation has resulted in eliminating or reducing COLA in Maine, Minnesota, New Jersey, Rhode Island, South Dakota, Colorado and others. The Arizona Supreme Court case of February, 2014 was an aberration because judges were included in the reform, and, traditionally, judges' salaries cannot be affected while they are sitting. However, there was in Arizona a favorable vote on a constitutional amendment regarding pension reform for firefighters statewide based on a consensual agreement to changes to an existing pension benefit enhancement similar to COLA reduction reforms in other states. The Illinois Supreme Court has ruled efforts to reduce COLA benefits for current employees violates the Illinois Constitutional Pension Clause.
4. Successful Illinois pension reform: Illinois Pension Legislation of 2010 for new employees as of January 1, 2011 was not seriously challenged and is effective. This created tier II for new employees with reduced pension benefits.

## IX. The Need for Uniform Pension Underfunding Disclosure and Whether Such Underfunding Is Crowding Out Funding of Essential Services and Needed Infrastructure

5. Pension reform declared unconstitutional: Illinois Pension Reform legislation in 2013, providing a claimed \$160 billion in savings over a 30-year period, was struck down by the Illinois Supreme Court as unconstitutional in the case of *In re Pension Reform Litigation* (Ill. Supreme Court, May 8, 2015, hereinafter "Ill. State Pension Reform Case"). The Supreme Court held the reform legislation was unconstitutional under the Illinois Pension Clause of the Illinois Constitution (Art. XIII § 5 hereinafter "Ill. Pension Clause") whereby, according to the Illinois Court, benefits accrue to the public worker once an individual begins work and becomes a member of a public retirement system and those contractual provisions cannot be impaired or diminished even in the face of a higher public purpose argument. "Membership in any pension or retirement system of the state, any unit of local government or school district, or any agency or instrumentality thereof, shall be an enforceable relationship, the benefits of which shall not be diminished or impaired." The Court held that there could be no exercise of police power to disregard the express provision of the Ill. Pension Clause, and the failure of the legislature to act consistent with the Pension Clause in the face of the well known need for funding of the unfunded pension obligations undermines the police power argument.

## IX. The Need for Uniform Pension Underfunding Disclosure and Whether Such Underfunding Is Crowding Out Funding of Essential Services and Needed Infrastructure

6. City pension reform denied: City of Chicago Labor Pension Reform litigation involving public laborers and workers (Ill. Supreme Court, March 24, 2016, hereinafter "City of Chicago Pension Reform Case") resulted in the Illinois Supreme Court ruling that the reforms were unconstitutional as a violation of the Ill. Pension Clause for the reasons set forth in the Illinois State Pension Reform case. The Court further found that the alleged consideration for the modification was already required funding and not sufficient to justify the change in benefits. Further, the Illinois Supreme Court ruled that Section 22-403 of the Illinois Pension Code in effect prior to 1970, which provided that the State of Illinois and City of Chicago were not obligated to fund more than the statutory required payment that the City had consistently funded, was superseded by the Ill. Pension Clause. The Supreme Court recognized the timing and amount of funding the pension obligation was a legislative power of the City that the Court could not then order or interfere with, and it was up to the City to decide the time and amount of funding.

## IX. The Need for Uniform Pension Underfunding Disclosure and Whether Such Underfunding Is Crowding Out Funding of Essential Services and Needed Infrastructure

---

7. San Jose and San Diego attempts: San Jose, San Diego and other cities have sought pension reform. San Jose's pension reform litigation recognized that pensions could be adjusted but, despite a 70% referendum, the court struck down portions of legislation as violating vested rights of workers. However, the court also recognized the City of San Jose's right and power to reduce salaries prospectively and to fire or lay off employees.
8. Austerity versus Reform: Some cities since 2007 have resorted to layoffs, furloughs, reduction in workforce and deferred preventive maintenance and infrastructure to deal with any issues related to insufficient funds to pay expenses including costs of labor and pension benefits.

## IX. The Need for Uniform Pension Underfunding Disclosure and Whether Such Underfunding Is Crowding Out Funding of Essential Services and Needed Infrastructure

---

F. What can be adjusted as to pension benefits: The non-impairment laws are not all-encompassing and generally have been held not to reach:

1. Benefits that accrue in the future.
2. Reduction in mandatory retirement age.
3. Reduction in hours or salary.
4. Loss of benefits for non-compliance with the plan.
5. Dismissal of public employee.

Even though such may indirectly affect the pension benefits received. (But see contrary discussion of the Illinois Supreme Court rulings above.)

## **IX. The Need for Uniform Pension Underfunding Disclosure and Whether Such Underfunding Is Crowding Out Funding of Essential Services and Needed Infrastructure**

---

### **G. Benefits of a uniform disclosure of pension funding and underfunding:**

1. GASB (GASB Statements 67 and 68) has promulgated some guidelines to help provide financial information concerning Pension Funding in a more organized and effective manner. The question raised is whether a more uniform approach with less variables would allow an apple to apple comparison and allow investors and the municipal market the ability to more effectively assess and compare the situation.



## IX. The Need for Uniform Pension Underfunding Disclosure and Whether Such Underfunding Is Crowding Out Funding of Essential Services and Needed Infrastructure

---

- H. Funding of underfunded pension obligations should not impair or limit full funding of essential services and needed infrastructure:
1. We cannot avoid economic cycles but history of financial stability points the way. In the U.S.A., financial challenges and difficulties in balancing a government budget is not so much caused by the desire to spend more than tax revenues currently generate but rather by economic cycles such as panics, recessions and depressions. This is exacerbated by unfunded pension obligations that are not sustainable and affordable as well as the adverse effects of failing to fund essential services and needed infrastructure at an acceptable level. The healthy economy of a state or local government goes hand in hand with full funding of essential services and needed infrastructure improvements and making sure all costs, including labor and pension obligations, are sustainable and affordable.

## IX. The Need for Uniform Pension Underfunding Disclosure and Whether Such Underfunding Is Crowding Out Funding of Essential Services and Needed Infrastructure

---

2. Need to address the systemic problems of the past that caused financial distress. Other countries that have suffered the need for a debt restructuring have generally repeated the process numerous times with band aids rather than a permanent fix because they merely reduced debt without addressing the systemic problems that caused the financial distress. States and local government should always strive for the permanent fix as opposed to the band aid.
3. Balanced budgets require services and infrastructure at the level desired. The state and local governments in the U.S.A. have a long history of financial credibility having learned that quick fixes and failure to maintain governmental services and infrastructure at an acceptable and desired level results in a loss of businesses and individual taxpayers with the accompanying fiscal distress.

## IX. The Need for Uniform Pension Underfunding Disclosure and Whether Such Underfunding Is Crowding Out Funding of Essential Services and Needed Infrastructure

---

4. The state legislatures have assisted in balancing the budget with needed legislation. State legislatures have assisted in balancing state and local governments by passing legislation that (i) limits debts and taxes, (ii) provides financial oversight and assistance to those who need it, (iii) assures and requires funding of needed services and infrastructure at the level desired, (iv) respects the principles of government financing and uses statutory liens and special revenues to reduce the cost of borrowing and reinvests in the state and local governments and (v) encourages reinvestment in the state and local governments and creation of new, good jobs and business development.

## IX. The Need for Uniform Pension Underfunding Disclosure and Whether Such Underfunding Is Crowding Out Funding of Essential Services and Needed Infrastructure

### I. The need to reinvest in state and local governments:

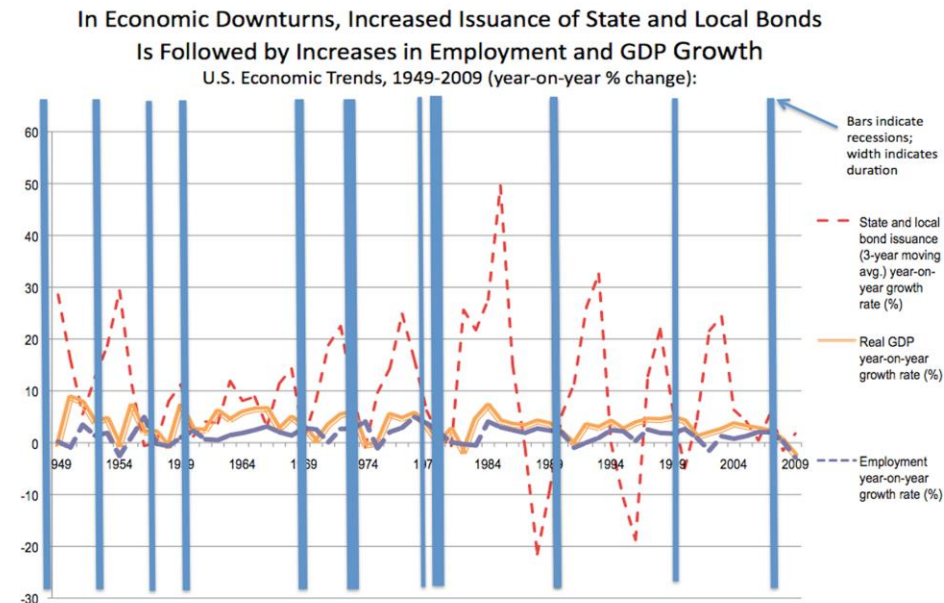
1. The \$3.6 trillion price tag and cost of delay. The American Society of Civil Engineers ("ASCE"), in its 2013 Report, estimates the cost to maintain infrastructure at a passable level will be \$3.6 trillion by 2020 or about 4 times the annual tax revenues for all state and local governments. In 2009, ASCE's number for the next 5 years was \$2.2 trillion. Inattention has caused the number to increase by \$1.4 trillion in 5 years. In ASCE's 2017 Report stated the cumulative infrastructure funding needs based on current trends extended to 2025 is \$4.59 trillion to have passable infrastructure estimated funding has a gap of over \$2 trillion. ASCE discovered in its 2016 economic study "Failure to Act Closing the Infrastructure Investment Gap for America's Economic Future" that the failure to do necessary infrastructure improvements in the U.S.A. will cost the country \$3.9 trillion in losses suffered to the GDP by 2025, \$7 trillion in lost business sales by 2025 and \$2.5 million in lost American jobs in 2025.

## **IX. The Need for Uniform Pension Underfunding Disclosure and Whether Such Underfunding Is Crowding Out Funding of Essential Services and Needed Infrastructure**

---

2. Historically state and local government increased reinvestment after economic downturn. Continued borrowing is required to fund needed infrastructure and stimulate the economy as demonstrated by increased borrowing of state and local governments after each economic downturn since 1949, except the last one (2008). In each case except for 2008, the real GDP and employment year to to year increased due in part to investment stimulus creating a recovery.

# IX. The Need for Uniform Pension Underfunding Disclosure and Whether Such Underfunding Is Crowding Out Funding of Essential Services and Needed Infrastructure



- American Society of Civil Engineers estimates that between 2016-2025 about \$4.5 trillion of infrastructure improvements must be made to keep U.S. infrastructure acceptable.
- For every dollar of hard cost of infrastructure improvement, \$3.21 of economic activity is generated over the course of 20 years.
- At least \$2 trillion of the \$4.5 trillion needs future financing. There is currently no estimated funding for it.
- For every new job created due to infrastructure improvements or economic development, there are at least 2 to 5 jobs produced indirectly in supplier industries and induced in local servicing industries.

# APPENDIX I – General Overview of a 50 State Survey of Rights and Remedies Provided by States to Investors Relating to Government Bond Debt and State Oversight and Supervision of Financial Emergencies and Authorization to File Chapter 9 Bankruptcy

GENERAL OVERVIEW OF MUNICIPAL INSOLVENCY PROVISIONS															
State	Municipal Bankruptcy Authorization	Debt Limitation	Municipal Restructuring Mechanism	Rec elever	Refunding Bonds	Other Default Resolution Remedies	Accounting	Foreclosure	Injunction	Mandamus	Other Remedies	Special Revenue Bonds	Statutory Lien SL-1*	Statutory Lien SL-2**	Statutory Lien SL-3***
ALABAMA	Y (bonds only)	X		X	X			X	X	X		X	X		
ALASKA	N				X	X (taxing limits; appointment of trustee)		X		X		X		X	
ARIZONA	Y	X	X (School District Receivership)	X	X	X (any action necessary for holders)		X		X	X (any action necessary)	X			
ARKANSAS	Y	X		X	X	X (taxing limits; appointment of an assessor)				X		X		X	
CALIFORNIA	Conditional (use of a neutral evaluator or declaration of fiscal emergency)	X	X (California Debt and Investment Advisory Commission)	X	X	X (negotiations; school district budget requirements)	X	X	X	X	X (bondholder action and any other action and special tax bonds)	X	X		
COLORADO	Limited	X		X	X		X		X	X	X (bondholder action)	X	X		
CONNECTICUT	Conditional	X	X (ad hoc state intervention)	X	X	X (appointment of a trustee; revenue set-aside)			X	X	X (bondholder action and contractual remedies)	X		X	
DELAWARE	N	X			X					X		X			
DISTRICT OF COLUMBIA	N	X	X (District of Columbia Financial Responsibility and Management Assistance Authority)		X		X		X	X	X (declare all bonds due and payable)	X			
FLORIDA	Conditional		X (Bond Financial Emergencies Act and Division of Bond Finance and Local Government Financial Technical Assistance Program)	X	X		X		X	X		X	X		
GEORGIA	N (specifically prohibited)	X	X (Georgia Local Government Financial Monitoring)	X	X	X (debt compromise)				X	X (court action to enforce collection)	X			

\* The language of the statute appears to strongly support a determination that it is a statutory lien

\*\* While the language of the statute may appear to create a statutory lien further clarification would be helpful to reaffirm the intent to create a statutory lien

\*\*\* While the language of the statute may appear to create a statutory lien it is insufficient and additional language is required to clarify the intent and to create a statutory lien. The language could be read as just providing for perfection of a pledge or lien without the intent and effect to create a statutory lien

# APPENDIX I – General Overview of a 50 State Survey of Rights and Remedies Provided by States to Investors Relating to Government Bond Debt and State Oversight and Supervision of Financial Emergencies and Authorization to File Chapter 9 Bankruptcy

HAWAII	N	X		X	X		X	X		X	X (bondholder action)	X			
IDAHO	Y	X	X (debt readjustment plans for certain districts)	X	X	X (Bond Guaranty Act)	X	X		X		X	X		
ILLINOIS	Limited	X	X (Financially Distressed City Law and Financial Planning and Supervision)	X	X			X	X	X	X (appropriate relief)	X	X	X	
INDIANA	N	X	X (Distressed Political Subdivision and Township Protections)	X	X	X (redemption bonds)	X	X	X	X		X	X	X	
IOWA	N, with exception	X		X	X	X (moratorium)				X		X	X	X	
KANSAS	N	X		X	X		X	X		X		X			
KENTUCKY	Conditional	X	X (county restructuring)	X	X	X (taxing limits; appointment of trustee)	X		X	X		X	X	X	
LOUISIANA	Conditional	X	X (appointment of Fiscal Administrator)	X	X	X (state taxing authority)		X		X		X		X	
MAINE	N	X	X (Board of Emergency Municipal Finance)	X	X	X (earmarking)		X		X	X (attachment and any action necessary)	X			X
MARYLAND	N	X		X	X					X		X		X	
MASSACHUSETTS	N	X	X (ad hoc state intervention)	X	X	X (state bond payment intervention)				X		X			X
MICHIGAN	Conditional	X	X (Emergency Financial Management and Local Government and School District Fiscal Accountability Act)	X	X					X		X	X	X	
MINNESOTA	Y	X	X (Back-Up Payment Procedures for Municipalities and School Districts)		X	X (school district expenditure limitations)				X	X (appropriate remedies to enforce bondholder rights)	X		X	
MISSISSIPPI	N	X		X	X	X (municipal borrowing)	X	X	X		X (other appropriate remedies)	X		X	
MISSOURI	Y	X		X	X		X	X		X	X (other appropriate remedies)	X			



# APPENDIX I – General Overview of a 50 State Survey of Rights and Remedies Provided by States to Investors Relating to Government Bond Debt and State Oversight and Supervision of Financial Emergencies and Authorization to File Chapter 9 Bankruptcy

MONTANA	Y, but not counties	X		X	X					X	X (limited remedy and interest penalty; suits in equity)	X			
NEBRASKA	Y	X		X	X	X (debt compromise)		X		X		X			
NEVADA	N	X	X (Local government Financial Assistance and Audit Enforcement Act)	X	X	X (third-party agreements)	X	X	X	X		X		X	
NEW HAMPSHIRE	N	X	X (Emergency Financial Assistance)	X	X					X	X (contractual remedies)	X			
NEW JERSEY	Conditional	X	X (Local Government Supervision Act; Municipal Rehabilitation and Economic Recovery Act of 2002 and Special Municipal Aid Act)	X	X	X (school district fiscal monitor and Casino Tax Property Stabilization Act)	X	X		X		X	X		
NEW MEXICO	N	X	X (financial auditing and emergency loans)	X	X	X (emergency loans from state)				X		X			
NEW YORK	Conditional	X	X (Emergency Financial Control Board, Municipal Assistance Corporation; New York Financial Control Board)	X	X	X (appointment of a trustee)	X	X		X		X	X		
NORTH CAROLINA	Conditional	X	X (local government debt monitoring; local government fiscal management)	X	X	X (local government commission)		X		X		X			X
NORTH DAKOTA	N	X		X	X		X			X		X			X
OHIO	Conditional	X	X (state auditor's fiscal caution and fiscal watch; fiscal emergencies; financial planning and supervision commission)	X	X		X	X	X	X	X (general remedies provision, including appointment of trustee and action to declare bonds not paid from property taxes immediately payable)	X			

# APPENDIX I – General Overview of a 50 State Survey of Rights and Remedies Provided by States to Investors Relating to Government Bond Debt and State Oversight and Supervision of Financial Emergencies and Authorization to File Chapter 9 Bankruptcy

OKLAHOMA	Y	X		X	X	X (settlement of debt)	X			X		X			
OREGON	Limited	X	X (County Public Safety Emergency and Fiscal Control Board; Municipal Debt Advisory Commission)	X	X	X (refunding bond cram-down)		X		X		X			X
PENNSYLVANIA	Conditional	X	X (Financially Distressed Municipalities Act; Intergovernmental Cooperation Act)	X	X	X (appointment of a trustee)	X			X		X	X		
PUERTO RICO	N	X	X (Puerto Rico Oversight, Management and Economic Stability Act)	X	X	X (first lien provisions)	X			X		X	X		
RHODE ISLAND	Conditional	X	X (fiscal overseer; municipal receiver; budget commission)	X	X	X (bond issuance requirements; bond payment guarantee)	X	X		X		X	X		
SOUTH CAROLINA	Y	X		X	X	X (state treasurer withhold of state appropriation)	X	X		X		X (any appropriate action)	X	X	
SOUTH DAKOTA	N	X		X	X					X		X		X	
TENNESSEE	N		X (financially distressed municipalities procedures)	X	X	X (emergency financial aid to local governments)	X			X		X		X	X
TEXAS	Y	X	X (municipal receivership)	X	X			X		X		X			X
UTAH	N	X		X	X					X		X (contractual remedies)	X		X
VERMONT	N	X		X	X			X		X		X			X
VIRGINIA	N	X	X (bond payment guarantee provisions)	X	X					X		X (any contractual remedy)	X		X
WASHINGTON	Y	X		X	X	X (designation of trustee)		X	X	X		X			
WEST VIRGINIA	N	X		X	X		X	X	X	X		X			
WISCONSIN	N	X	X (Deficiency Protection for Public Improvement Bonds)		X			X		X		X			
WYOMING	N	X		X	X		X	X	X	X		X			
Total		49	30	47	52	29	24	28	15	52	18	52	16	15	10

\*\*\*\* These numbers include both the District of Columbia and Puerto Rico where applicable and totals may differ from other materials that only review 50 states.

---

The services of Chapman Strategic Advisors LLC do not include legal services and the protections of the client-lawyer relationship will not exist. Only Chapman and Cutler LLP can provide legal services, if retained pursuant to a separate engagement agreement with a client. This document has been prepared by Chapman Strategic Advisors LLC for informational purposes only. It is general in nature and based on authorities that are subject to change. It is not intended as a recommendation or advice with respect to municipal financial products or the issuance of municipal securities. Accordingly, readers should consult with, and seek the advice of, their own independent registered municipal advisor with respect to any individual situation that involves the material contained in this document, the application of such material to their specific circumstances, or any questions relating to their own affairs that may be raised by such material.

© 2019 Chapman Strategic Advisors LLC