TAXES AND ABILITY TO PAY IN MUNICIPAL BANKRUPTCY

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Abstract: Scholars and commentators have argued that municipalities can and should use bankruptcy to shed unwanted liabilities, particularly employee healthcare and pension commitments. Courts increasingly have agreed: Detroit’s approved bankruptcy plan cut pensions, and the bankruptcy court overseeing the bankruptcy of Stockton, California brought down barriers to pension-cutting. Both courts found their way around state provisions arguably protecting municipal pensions.

Now that pension-cutting in bankruptcy has momentum, we can expect to hear arguments for using bankruptcy not just in cases like Detroit and Stockton where the municipality cannot meet all its obligations, but also in cases where residents or politicians come to regret municipal promises to workers.

This Article presents the most sustained, straightforward, and comprehensive argument to date that existing law requires bankruptcy courts to provide relief only when municipalities are reasonably unable to meet their obligations. The legislative history of the municipal bankruptcy statutes consistently sounds this theme, and judicial precedents are in agreement.

Congress did not provide a clear standard for courts to apply when looking at tax levels in municipal bankruptcy. Although the legislative history and case law provide some support for the proposition that municipalities should be required to tax at the level that maximizes revenue, the Article suggests a more moderate criterion: absent a compelling explanation, courts could require that a municipality tax at the top of its peer group as a condition of bankruptcy eligibility and plan confirmation.

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INTRODUCTION

New life suffuses American municipal bankruptcy. For nearly eighty years, filings were rare and large filings nonexistent. Municipal bankruptcy was not even covered in leading bankruptcy casebooks, and

1. See Juliet M. Moringiello, Chapter 9 Plan Confirmation Standards and the Role of State Choices, 37 CAMPBELL L. REV. 71, 72 (2015) (“Since municipal bankruptcy first entered federal law in 1934, fewer than 700 cases have been filed.”).
2. Compare ELIZABETH WARREN & JAY LAWRENCE WESTBROOK, THE LAW OF DEBTORS AND
commentators regularly questioned its usefulness. But recently every year has seemed to bring a new superlative for bankruptcy: Jefferson County, Alabama’s bankruptcy was the largest by dollar amount when it was filed in 2011. In 2012, Stockton, California became the largest city by population ever to have sought bankruptcy protection, only to be surpassed in 2013 when Detroit’s filing riveted the eyes of the nation on a process that led to a “Grand Bargain,” which reached far beyond the municipal limits to the halls of the country’s best-known and most prestigious cultural foundations.

After the resolution of the Stockton and Detroit cases, municipal bankruptcy is part of the new normal: In California, San Bernardino lingers in bankruptcy while Vallejo reportedly teeters on the edge of a


second filing.\textsuperscript{8} Atlantic City, New Jersey threatens to become the first New Jersey municipality to enter bankruptcy since the Great Depression.\textsuperscript{9} And mighty Chicago could eclipse even the Detroit bankruptcy.\textsuperscript{10}

This reinvigoration of bankruptcy coincides with a change in the standard image of the archetypal municipal creditor: once seen as a distant bondholder, now more and more the creditor is identified as a retired worker.\textsuperscript{11} The unsustainability, real or apparent, of municipal pensions and health care benefits has emerged as a favorite topic not just of bond analysts,\textsuperscript{12} but also of organizations charged with promoting the broader public interest.\textsuperscript{13} The idea that public pensions are too high has taken a firm hold in discourse, even though some recent prophecies of imminent municipal financial collapse have not materialized as

\textsuperscript{11}See infra Section I.B.
\textsuperscript{12}See, e.g., Janney Capital Markets, Are Pension Obligation Bonds as Bad as Some Critics Say?, MUN. BOND MKT. MONTHLY, May 1, 2015, at 1, 2 (calling attention to “[c]redit deterioration and/or negative rating actions . . . in the states of Kansas, Kentucky, and Pennsylvania partly as a result of dwindling pension assets (mostly because of underfunding) when compared to rising liabilities”); Janney Capital Markets, Municipal Bond Market Credit Analyst Survey - First Annual, MUN. BOND MKT. MONTHLY, Apr. 6, 2015, at 1 (“The most important issue/trend facing the municipal bond market is currently Public Pensions . . . . 86% of municipal credit analysts polled included the category in their top five, according to our survey results.”).
\textsuperscript{13}See PEW CHARITABLE TRUSTS, A WIDENING GAP IN CITIES: SHORTFALLS IN FUNDING FOR PENSIONS AND RETIREE HEALTH CARE 38 (2013), http://www.pewtrusts.org/~media/legacy/uploadedfiles/pcs_assets/2013/Pewcitypensionsreportpdf.pdf [https://perma.cc/LNS2-7EYV] (“For a number of America’s largest cities, the bill for public sector retirement benefits already threatens strained budgets. And more pressures are on the horizon as unpaid pension bills in a variety of sizes, as well as retiree health costs, continue to accumulate.”).
predicted. Municipal bankruptcy as process and retiree as creditor come together in recent decisions upending the longstanding conventional wisdom that public pensions cannot be cut in bankruptcy. The trend started small, when a bankruptcy judge in October 2012 approved a plan of adjustment for the tiny city of Central Falls, Rhode Island that included pension cuts of up to fifty-five percent. Things got serious when the Detroit bankruptcy court held—despite a pension-protecting state constitutional provision—that city pensions could be impaired and then approved a plan of adjustment that reduces general employee pensions by 4.5%. The third decision—the one that makes a trend—came from California, where the court overseeing the Stockton bankruptcy rejected arguments that pensions administered by the state’s gargantuan California Public Employees’ Retirement System (CalPERS) could not be impaired. Although Stockton did not actually try to impair pensions in its plan of

14. For example, in December 2010, analyst Meredith Whitney stated on the television news program 60 Minutes that there could be 50 to 100 or more “sizable” municipal bond defaults and that defaults “will amount to hundreds of billions of dollars” and that the predicted cataclysm would be “something to worry about within the next twelve months.” Steve Kroft, State Budgets: Day of Reckoning, 60 MINUTES (Dec. 19, 2010), at 12:36–12:38, 13:12–13:15, http://www.cbsnews.com/videos/state-budgets-day-of-reckoning/ [https://perma.cc/5FEM-B94Q]. Nothing approaching this scale of default has yet occurred. For example, total reported debts in the Detroit bankruptcy were $18 billion. Chris Christoff, Detroit’s Record $18 Billion Bankruptcy Will End Tonight, BLOOMBERG (Dec. 10, 2014), http://www.bloomberg.com/news/articles/2014-12-10/detroit-asks-to-end-record-municipal-bankruptcy-snyder-says-1 [https://perma.cc/GHG6-2LVC].

15. See, e.g., David A. Skeel, Jr., Can Pensions Be Restructured in (Detroit’s) Municipal Bankruptcy? 1 (Univ. of Pa. Law Sch., Research Paper No. 13-33, 2013) (“As recently as five years ago, conventional wisdom held that political and legal obstacles made it impossible to restructure pensions in bankruptcy.”).


19. In re City of Stockton, 526 B.R. 35, 55–60 (Bankr. E.D. Cal. 2015) (rejecting arguments that CalPERS pension impairment is impeded by California “vested rights” doctrine, California statute forbidding rejection of CalPERS servicing contracts, and California statute providing for lien on municipal assets upon termination of CalPERS servicing contract, and suggesting that “executory municipal pension plans” could be modified under the standards set by the Supreme Court for rejection of collective bargaining agreements in NLRB v. Bildisco & Bildisco, 465 U.S. 513 (1984)). The Ninth Circuit Bankruptcy Appellate Panel dismissed an appeal of the Stockton decision, primarily on the ground that the appeal was equitably moot. Franklin High Yield Tax-Free Income Fund v. City of Stockton (In re City of Stockton), 542 B.R. 261, 278 (B.A.P. 9th Cir. 2015).
adjustment, the decision may be even more significant than the Detroit decision because of the sheer size of the system in question. And even though California public pensions have not been cut to date, both the Vallejo and the Stockton bankruptcies featured cuts to retiree health benefits.

Because municipal bankruptcy is becoming more viable in general, cities might be expected to try to employ their newly useful tool in more situations. In particular, municipalities might decide to use bankruptcy not just when they face otherwise unfixable fiscal emergencies, but whenever they find it, on balance, desirable to impair creditors. And the growing perception that municipal retirees’ benefits are too high suggests that pensions and health benefits may be the target of a new round of municipal bankruptcies, motivated by a desire not to raise taxes to meet existing commitments.

This Article argues that Congress did not intend for municipal bankruptcy to be used in such a way. A review of the legislative history of the municipal bankruptcy statutes—six in all contain relevant history—shows that Congress consistently intended, from the first acts in the 1930s through the last relevant enactment in the 1980s, that municipalities use bankruptcy only when they could not reasonably pay their debts. 

20. Indeed, non-pension creditors complained in their unsuccessful appeal they were the victims of unfair discrimination in light of the failure to impair pensions. See Opening Brief of Appellants at 2, 57–62, Stockton, 542 B.R. 261 (No. EC-14-1550). In San Bernardino, it appears that the city’s recent Plan of Adjustment follows Stockton in impairing retiree health benefits but not pensions. See Disclosure Statement with Respect to the Plan for the Adjustment of Debts of the City of San Bernardino, California at 7, San Bernardino City Prof’l Firefighters Local 891 v. City of San Bernardino (In re City of San Bernardino), 545 B.R. 14 (Bankr. C.D. Cal. 2015) (No. 12-bk-28006-MJ).


23. Stockton, 526 B.R. at 60 (“One result of this case is that the City terminated its program for lifetime retiree health benefits valued . . . at nearly $550 million for existing retirees.”).

24. Municipal bankruptcy, unlike other forms of bankruptcy, does require insolvency as a prerequisite for filing, but as discussed below it is not clear how much of a barrier this requirement really is to the determined municipality.

25. The 1994 Orange County bankruptcy may be an exception. See MARK BALDASSARE, WHEN GOVERNMENT FAILS: THE ORANGE COUNTY BANKRUPTCY 159–64 (1998) (describing failure of property tax increase proposed to help resolve Orange County bankruptcy and resulting media description of county residents as “wealthy ‘deadbeats’ who refused to pay their bills”). However, it
pay, not for municipalities that just do not want to pay.

Moreover, the history demonstrates that tax increases, and not just spending cuts, were to be on the table as means of achieving solvency. If anything, Congress has shown greater interest in tax increases than in spending cuts in debates over the prerequisites for relief in municipal bankruptcy. Municipal bankruptcy is not a way to ensure that budgets are balanced by spending cuts\textsuperscript{26} instead of tax increases.\textsuperscript{27}

The relatively sparse case law on municipal bankruptcy buttresses the argument. Courts have relieved cities like Central Falls,\textsuperscript{28} Detroit,\textsuperscript{29} Vallejo,\textsuperscript{30} Stockton,\textsuperscript{31} and San Bernardino\textsuperscript{32} that credibly showed they

\begin{itemize}
  \item seems possible that the bankruptcy resulted from a misunderstanding of the law so the case may be of limited relevance. \textit{See id.} at 111–12. In filing for bankruptcy protection, the supervisors’ intention was to prevent a run on the [Orange County] investment pool by freezing the funds in the pool, thus preventing the local government investors from withdrawing their money and the Wall Street firms from taking any more of the securities that they held as collateral . . . . But there were allowances in the bankruptcy [code] that seemed to exclude the reverse repurchase agreements between the Wall Street firms and the county treasurer. (\textit{New York Times}, 1994a). In fact, many Wall Street firms withdrew their collateral . . . . [Four firms] all sold collateral in the days right after the bankruptcy . . . . [It] is clear that the bankruptcy filings did not have the intended impact of stopping the Wall Street firms from withdrawing the collateral. \textit{Id.} at 111–12.


27. \textit{Cf.} Adam J. Levitin, \textit{Bankrupt Politics and the Politics of Bankruptcy}, 97 \textit{CORNELL L. REV.} 1399, 1458 (2012) (criticizing proposals for allowing states to seek bankruptcy protection: “[w]ith state bankruptcy proposals, however, the Rawlsian veil of legislation becomes embarrassingly threadbare. There is no doubt whose ox is to be gored by state bankruptcy: it is that of organized labor. Public employees’ unions, not municipal bondholders or taxpayers, are the clear target of state bankruptcy. State bankruptcy proposals make no pretense of even being a means of mitigating the procyclical fiscal problems facing states”).

28. \textit{See} Grace Wyler, \textit{Central Falls Files for Bankruptcy After Union Fails to Agree to Pension Cuts}, BUS. INSIDER (Aug. 1, 2011, 1:07 PM) (quoting state-appointed receiver Robert Flanders as saying, “[s]ervices have been cut to the bone . . . taxes have been raised to the maximum level allowable”).


30. \textit{See} Int’l Ass’n of Firefighters, Local 1186 v. City of Vallejo (\textit{In re City of Vallejo}), 408 B.R. 280, 294 (B.A.P. 9th Cir. 2009), aff’g \textit{In re City of Vallejo}, No. 08-26813-A-9, 2008 WL 4180008 (Bankr. E.D. Cal. Sept. 5, 2008) (describing the low level of services provided in Vallejo at time of its bankruptcy filing).

31. \textit{See In re City of Stockton}, 493 B.R. 772, 789–90 (Bankr. E.D. Cal. 2013) (describing Stockton’s “service delivery insolvency” and infeasibility of property tax increases in light of California’s Proposition 13); Joanne Lau, \textit{Modifying or Terminating Pension Plans Through Chapter 9 Bankruptcies with a Focus on California}, 40 \textit{FORDHAM URB. L.J.} 1975, 1976–77 (2013) (detailing Stockton’s high crime rate and arguing that “[c]itizens who are able to leave the city are doing so as a result”); \textit{see also} discussion \textit{infra} Section III.A.

32. \textit{See In re City of San Bernardino}, 499 B.R. 776, 787 (Bankr. C.D. Cal. 2013) (“[A]fter taking steps to cut costs and raise revenue, the City—faced with a 45.9 million dollar cash deficit—had
were in deep, bona fide distress and could not raise revenues by raising taxes.\textsuperscript{33} Courts have denied relief to municipalities that could have raised taxes to meet their obligations.\textsuperscript{34} And in Stockton at least, the court found the city eligible for bankruptcy as a way of making revenue increases feasible.\textsuperscript{35}

The policy against opportunism finds expression in at least four different statutory provisions: the requirement that municipalities be insolvent\textsuperscript{36} to commence a bankruptcy case, the requirement that cases and plans\textsuperscript{37} be filed in good faith, and the requirements that bankruptcy plans be “in the best interests of creditors”\textsuperscript{39} and be “fair and equitable”\textsuperscript{40} to dissenting classes of creditors.

To be sure, it could be argued that conditioning bankruptcy relief on the city’s achieving a particular tax level impermissibly invades the city’s (or state’s) authority, and thus violates the Bankruptcy Code (Code) or the Tenth Amendment to the Constitution.\textsuperscript{41} But it does not appear that any court has embraced such an argument, and the legislative history suggests that any such concern is cured by the fact that the court is simply applying conditions to relief that the bankrupt municipality is affirmatively seeking.\textsuperscript{42} Although it is conceivable, particularly after \textit{National Federation of Independent Business v. Sebelius},\textsuperscript{43} that the doctrine of unconstitutional conditions could bar courts from considering tax levels as part of determining whether to grant relief, courts that consider tax levels are not changing the terms of entrenched programs. Nor are they threatening a reduction in federal financial benefits

\textsuperscript{33} For general discussion of the poor health of municipally distressed cities, see generally Anderson, \textit{supra} note 26, at 1130–51.


\textsuperscript{35} \textit{Stockton}, 493 B.R. at 790.


\textsuperscript{37} \textit{Id.} § 921(c).

\textsuperscript{38} \textit{Id.} § 901(a) (incorporating 11 U.S.C. § 1129(a)(3) (2012) into Chapter 9); \textit{id.} § 1129(a)(3) (requiring that plan be filed in good faith).

\textsuperscript{39} \textit{Id.} § 943.

\textsuperscript{40} \textit{Id.} § 901 (incorporating 11 U.S.C. § 1129(a)(1) into Chapter 9); \textit{id.} § 1129(a)(1) (requiring that a plan be fair and equitable to dissenting creditor classes).

\textsuperscript{41} \textit{See infra} Section IV.A.

\textsuperscript{42} \textit{See infra} Section IV.A.

\textsuperscript{43} ___ U.S. ___, 132 S. Ct. 2566 (2012).
anywhere near as large as the reduction the states faced in Sebelius.44

Although it seems clear that Congress wanted bankruptcy courts to take tax levels into account in municipal bankruptcy, it is less clear just how they are supposed to do so. The Article evaluates three possible specific criteria that bankruptcy courts could use, each of which has some support in the legislative history, case law, or both. The first can be called “top-of-the-hill” criterion;45 this criterion would require that the municipality tax at the revenue-maximizing level as a condition of bankruptcy eligibility or plan confirmation. The second is the “share-some-pain” criterion, which has some support in the Stockton case. Under this criterion, relief would be conditioned on imposing a substantial tax increase. The third criterion is called the “top-of-the-range.” This criterion would require that the debtor tax at the top of a range of comparable municipalities.

None of the criteria is perfect, but the Article suggests that a combination of the three criteria has merit: a municipality could be required to tax at the top of the range absent an adequate explanation. One adequate explanation, based on the top-of-the-hill criterion, would be that taxing at the top of the range would actually reduce revenue. Another possible explanation, related to the share-some-pain criterion and embraced in the Stockton case, would be that the bankruptcy itself will enable revenue increases to pay creditors. Although the top-of-the-range criterion will engender debate, particularly over what municipalities are “comparable” to the debtor, it implements the congressional will in a way that is familiar to legal actors; peer-group comparisons are already widely used in the law.

This Article is not the first to suggest that bankruptcy courts should condition relief on tax increases to combat municipal opportunism. Professor Clayton Gillette has made that argument consistently.46 It is,
however, the first to bring to bear a comprehensive review of the legislative history and case law of municipal bankruptcy. It is also the first to consider and evaluate specific tests the bankruptcy court might use in determining just how high municipal taxes must be before a municipality can invoke the federal bankruptcy power to reduce its debts.

I. SETTING THE TABLE: MUNICIPAL BANKRUPTCY LAW AND THE POTENTIAL SUBSTITUTION OF BANKRUPTCY FOR REVENUE

This Part provides the background for the Article’s argument. First, it gives a brief overview of the history of municipal bankruptcy and relevant major provisions of Chapter 9 of the Bankruptcy Code. Second, it describes the increasing likelihood that municipal bankruptcy will be used to avoid raising sufficient revenue to meet obligations, particularly obligations to municipal retirees.

A. Brief History and Overview of Relevant Municipal Bankruptcy Law

Chapter 9 of the Bankruptcy Code governs municipal bankruptcy. Congress enacted the first municipal bankruptcy statute in 1934. Two years later, in Ashton v. Cameron County Water Improvement District, the Supreme Court ruled the 1934 Act unconstitutional. Congress quickly responded with a new statute in 1937. Commentators have noted that differences between the 1934 and 1937 Acts were small, and the 1937 Act was challenged on the same basis as the 1934 Act: it was

Gillette & David A. Skeel, Jr., Governance Reform and the Judicial Role in Municipal Bankruptcy, 125 YALE L.J. 1150, 1154 (2016) (citing McConnell & Picker, supra note 3); McConnell & Picker, supra note 3, at 466 (“[U]nsecured creditors of municipalities are protected from the moral hazard problem of opportunistic bankruptcy filings . . . by the best interests of the creditors standard.”).

47. Omer Kimhi reviews the legislative history of municipal bankruptcy in support of an argument that the 1976 Act marked an important change in the purpose of the statute from solving the “holdout problem” to providing comprehensive relief to cities on the model of corporate bankruptcy. Kimhi does not discuss tax increases as a condition for bankruptcy relief. See Kimhi, Solution in Search of a Problem, supra note 3, at 362–69.


50. 298 U.S. 513 (1936).


argued that the Act impermissibly gave the federal courts power over state affairs. The Court rejected this challenge in 1940 in United States v. Bekins. The change probably reflects a switch in the Court’s attitude more than any change in the Act’s content.

The 1934 and 1937 Acts were both styled as temporary emergency legislation to deal with the Depression and the 1937 Act was set to expire in 1940. Congress extended the life of the Act in 1940 and 1942 and made municipal bankruptcy permanent in 1946.

There were no major changes in municipal bankruptcy law until 1976, when Congress enacted a revised bankruptcy statute, the 1976 Act, which was intended to be more useful in handling large municipal bankruptcies. Given that major revision in 1976, municipal bankruptcy received comparatively little attention in the comprehensive 1978 Bankruptcy Act, although the 1978 Act did result in municipal bankruptcy’s current designation as Chapter 9 of the Code. Congress next made significant changes to municipal bankruptcy in 1988; the 1988 Act was primarily aimed at preserving the status of revenue bonds in municipal bankruptcy. The last noteworthy revision to the municipal bankruptcy statute was in 1994; the 1994 Act covered a large number of miscellaneous bankruptcy topics and resolved a split in authority by providing that municipal bankruptcy had to be specifically

53. 304 U.S. 27 (1938). Supreme Court authority on municipal bankruptcy is quite sparse. Apart from Ashton and Bekins, the only major case is Faitoute Iron & Steel Co. v. City of Asbury Park, 316 U.S. 502 (1942), which held that a state statute providing for composition of debts did not violate the Contracts Clause. Id. at 512–16. Congress prohibited state composition statutes that purport to bind non-consenting creditors in the 1946 Act. Act of July 1, 1946, Pub. L. No. 79-481, § 83(i), 60 Stat. 409, 415 (codified at 11 U.S.C. § 903(1)–(2) (2012)).


62. See, e.g., 6 Collier on Bankruptcy, supra note 52, § 900.LH[5], at 900-32 to -33 (1988 Amendments addressed the issue that “the postpetition lien termination provision (section 552) and the protection of nonrecourse secured creditors embodied in section 1111(b) . . . had the likely effect of converting nonrecourse revenue bonds into unsecured general obligation bonds”).

authorized by the municipality’s state government.  

Municipal bankruptcy under Chapter 9 differs from other bankruptcy proceedings in several ways. There are unique eligibility requirements: the debtor must be a municipality, must be specifically authorized under state law to seek bankruptcy protection, must be insolvent, and must desire to effect a plan of debt adjustment. The debtor generally must negotiate in good faith with its creditors prior to filing unless doing so is impracticable. There is no provision for involuntary municipal bankruptcy.

Once the municipality is in bankruptcy, the Code limits the court’s power in ways specific to that context. For example, Article 9 preserves the state’s power “to control, by legislation or otherwise, a municipality . . . in the exercise of [its] political or governmental powers,” and generally forbids the court, without the debtor’s “consent[]” from “interfer[ing] with (1) any of the political or governmental powers of the debtor; (2) any of the property or revenues of the debtor; or (3) the debtor’s use of enjoyment of any income-producing property.”

The Code contemplates that the case will be resolved by a plan of adjustment filed by the debtor. A plan cannot be confirmed unless certain requirements are met. First, the debtor must not be prohibited by law from taking any action necessary to carry out the plan. Second, the debtor must obtain any regulatory or electoral approval necessary under non-bankruptcy law to carry out the plan, or the relevant plan provisions must be conditioned on receipt of such approval. Third, the

64. Id. § 402, 108 Stat. at 4141 (codified at 11 U.S.C. § 109(c)(2) (2012)).
66. Id. § 109(c)(2).
67. Id. § 109(c)(3).
68. Id. § 109(c)(4).
69. Id. § 109(c)(5)(B), (C). A debtor may file under Chapter 9 without fulfilling this requirement if it has actually obtained the approval of creditors holding a majority in amount of the claims in each class that the debtor intends to impair, id. § 109(c)(5)(A), or if the debtor reasonably believes that a creditor may seek to obtain an avoidable transfer, id. § 109(c)(5)(D).
70. Id. § 903.
71. Id. § 904.
72. Id. § 904(1)–(3).
73. Id. § 941. Unlike Chapter 11, Chapter 9 makes no provision for anyone other than the debtor to file a bankruptcy plan.
74. Id. § 943.
75. Id. § 943(b)(4).
76. Id. § 943(b)(6).
plan must be feasible and in the best interests of creditors.\textsuperscript{77} If the plan is to be crammed down (that is, approved over the objection of a class of creditors), the plan must, with respect to each class of impaired claims, be fair and equitable, and not discriminate unfairly.\textsuperscript{78}

\textbf{B. The Potential Substitution of Bankruptcy for Revenue}

There is a real and growing possibility that municipalities will start to use bankruptcy as an alternative to raising taxes to meet obligations, particularly retiree pension and healthcare obligations.

One reason for this possibility is that municipal debt in general, and retiree benefits in particular, is increasingly called “unsustainable.”\textsuperscript{79} The term “unsustainable” can mean different things. For example, a municipal debt could be called “unsustainable” if it could not be paid out of existing tax revenues, even if the debt could be paid with tax increases. For some, the category of “unsustainable” debt apparently includes all traditional, defined-benefit pension plans,\textsuperscript{80} or even all compensation arrangements that result from collective bargaining agreements.\textsuperscript{81} Richard Epstein links the asserted unsustainability of public employment contracts to their asserted unfairness:

\begin{quote}
[I]t is a high moral imperative that someone, somehow, has to find a way to undo all the one-sided contracts that national,
\end{quote}

\textsuperscript{77. Id. § 943(b)(7).}

\textsuperscript{78. Id. § 901(a) (incorporating § 1129(b)(1) by reference); id. § 1129(b)(1) (imposing “fair and equitable” and “no unfair discrimination” requirements with respect to impaired classes of claims).}

\textsuperscript{79. For example, a Westlaw search of Law Reviews & Journals on June 23, 2015, on “pension /s unsustainable” turned up 46 results, 35 of them from 2010 or later. A search of articles via Google News that discuss both “unsustainable” and “pensions” turns up 41,800 results (Feb. 9, 2016). The same search of news sources via Lexis Advance from Jan. 1, 2005, to date came up with over 35,000 results (with a sharp rise starting in 2008 and a peak at 2011 that has plateaued until today). Site searches of leading national think tanks also turned up numerous results: Heritage Foundation (165), American Enterprise Institute (334), Brookings Institution (447) and Center on Budget and Policy Priorities (76).

\textsuperscript{80. WAYNE H. WINEGARDEN, GOING BROKE ONE CITY AT A TIME: MUNICIPAL BANKRUPTENCIES IN AMERICA 20–21 (2014) (“Defined Benefit (DB) plans are unwise, unsustainable, and should be replaced with Defined Contribution (DC) plans.”). One recent student comment describes defined contribution plans in general as a “more sustainable model” than defined benefit plans, and discusses “state-authorized local tools” for dealing with pensions for three pages without ever mentioning even the theoretical possibility of tax increases. Hannah Heck, Comment, Solving Insolvent Public Pensions: The Limitations of the Current Bankruptcy Option, 28 EMORY BANKR. DEV. J. 89, 113–16, 128 (2011).

\textsuperscript{81. Richard W. Trotter, Running on Empty: Municipal Insolvency and Rejection of Collective Bargaining Agreements in Chapter 9 Bankruptcy, 36 S. ILL. U. L.J. 45, 50 (2011) (stating without qualification that “[t]he collective bargaining agreements between municipalities and public sector workers are not sustainable under the current fiscal framework”).}
state, and local governments have entered into with their unionized workforces, which call for a set of unsustainable pension and health care obligations. The claim that workers have rights to perpetuate these one-sided arrangements ignores the intolerable financial burdens that these outsized contracts impose on everyone else.82

At the same time that the idea that local retiree benefits are unsustainable is gaining ground, bankruptcy is becoming more and more established as a way of adjusting municipal debts. Residents might vote out elected officials who take a municipality into bankruptcy, but this risk to political careers should decrease as bankruptcy becomes more acceptable. As Warren Buffett puts it, “the stigma [of municipal bankruptcy] has probably been reduced” by recent filings,83 and the apparent success of bankruptcy proceedings in Detroit and Stockton can only have reduced the stigma still further. Against this backdrop, it is natural for those who want to balance budgets without raising taxes to look to bankruptcy as a way of accomplishing their goals. Reducing debts, even those that the municipality can afford to pay, will be attractive to those who would like to continue enjoying amenities without tax increases.84 Focusing on pension debts in particular will be attractive for those who think that defined-benefit pension plans are unsustainable or believe that public employee pay packages are illegitimate.

Indeed, scholars already have called for relaxing the insolvency requirement for municipal bankruptcy, one of the major statutory obstacles to opportunistic filing. David Skeel argues that “a lot of cities who might be good candidates for Ch. 9 are going to have trouble meeting that insolvency standard” and that “[w]e do not use that standard for other bankruptcies.”

This call to make it easier for cities to get into bankruptcy is particularly noteworthy both because of Skeel’s prominence as a critic of “unsustainable” debt and because he has elsewhere recognized that public debt is not unsustainable if taxes can be levied to pay it. This leading commentator seems to be moving toward the position that cities should be able to use bankruptcy as a substitute for increasing tax revenues.

The changing status of municipal bankruptcy has not escaped the notice of financial professionals. One municipal bond analyst recently discussed “taxpayer groups who are looking to get into bankruptcy just to shed debt.”

Although that analyst thought that the Jefferson County bankruptcy plan, which included large sewer rate increases, did “take the thunder out” of these groups’ claims, at least temporarily, no one

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86. See Skeel, Jr., supra note 15, at 8 (“[I]t is difficult or impossible to restructure accrued obligations outside of bankruptcy under Michigan law, even if they appear to be unsustainable.”); David A. Skeel, Jr., Is Bankruptcy the Answer for Troubled Cities and States?, 50 HOUS. L. REV. 1063, 1084 (2013) (“[A] major piece of the puzzle for many of the most troubled municipalities and states is unsustainable pension promises.”); David A. Skeel, Jr., When Should Bankruptcy Be an Option (for People, Places, or Things)?, 55 WM. & MARY L. REV. 2217, 2231–33 (2014) (arguing that one factor relevant to whether bankruptcy relief should be available in general is whether “unsustainable debt” is a problem in a given situation).

87. David A. Skeel, Jr., States of Bankruptcy, 79 U. CHI. L. REV. 677, 688 (2012) (arguing that “thanks to taxes and other revenues, [states] may be able to handle debt burdens that initially appear to be oppressive”). In the same vein, see Skeel, Jr., supra note 15, at 13 (in analyzing pension restructuring in bankruptcy under the Takings Clause, “the pertinent question is what an investor’s expectations would be for an underfunded pension in a time of financial crisis, not expectations in ordinary times” (emphasis added); id. at 15 (“So long as only financially stressed municipalities are permitted to file for bankruptcy, the best interests protection minimizes any interference with the Contracts Clause”); id. at 23 (argument that best-interests clause prohibits restructuring of Detroit pensions “is flawed, because it assumes that Detroit could plausibly come up with the money to pay its pensions in full. It is more likely that Detroit would have simply stop[ped] paying its pensions at some point. Given this possibility, the best interests test will not be interpreted as prohibiting any restructuring of pensions”).


89. Id.
decision can put to rest the debate over municipal taxes and debt, including pensions.

Some commentators, including Professor Kevin Kordana, have asserted that financial markets will discipline municipalities, so that opportunistic filings are not a risk. But a bankruptcy targeted at workers would not necessarily harm financial creditors—for example, certain obligations, such as revenue bonds, could be paid through the bankruptcy. Or a municipality might not have any, or much, capital-market debt. Or its pension obligations might dwarf its capital-market debt, so that the cost of capital-market discipline would be small relative to the benefit of relief from pension obligations. Moreover, capital markets may not provide much discipline anyway: credit rating agencies have well-known problems, and diversification and hedging can blunt the incentives for fine-grained monitoring.

II. TAXES AND MUNICIPAL BANKRUPTCY: LEGISLATIVE HISTORY

Chapter 9 of the Bankruptcy Code does not in so many words address any obligation municipalities may have to raise taxes as a condition of bankruptcy relief. However, as discussed in more detail below, at least four provisions of the Code arguably bear on the matter. The legislative history of municipal bankruptcy sheds light on the ambiguous statutory text. The Article addresses the legislative history first to put the somewhat abstract statutory terms in context.

The legislative history of the municipal bankruptcy statutes, starting

90. See Kevin A. Kordana, Tax Increases in Municipal Bankruptcies, 83 Va. L. Rev. 1035, 1071–89 (1997) (arguing by analogy to sovereign debt that the need to return to the capital markets is likely to prevent municipalities from opportunistically defaulting); David L. Dubrow, Chapter 9 of the Bankruptcy Code: A Viable Option for Municipalities in Fiscal Crisis?, 24 Urb. Law. 539, 586 (1992) (“It is clear that a municipality filing . . . under Chapter 9 would take such a decision extremely seriously and would be very concerned about the municipality’s future standing in the credit markets. Frivolous filings are not the danger.”).


93. See discussion infra Part 0

with the 1934 Act, makes clear that Congress had an abiding concern with making sure that municipalities paid creditors all they were reasonably able to pay. The legislative record also suggests that the concept of “ability to pay” included ability to pay through raising taxes. Finally, although the first municipal bankruptcy law took shape before the current era of direct democracy in local taxation, the record suggests that Congress was concerned about opportunism on the part of local populations, so that the voters’ failure to approve a tax increase would be cause for denying relief in Chapter 9. The statutes enacted in the “modern” era of municipal bankruptcy, 1976 and beyond, did not depart from the original understanding. Indeed, the legislative history of the 1976, 1978, and 1988 Acts expressly called upon municipalities to exercise their taxing power to the fullest extent to meet their obligations and affirmed judicial precedents under the older statutes that imposed a similar obligation.

A. “Maximum Capacity to Pay”: The 1934, 1937, and 1946 Acts

The first three municipal bankruptcy statutes reflect a continuing concern that municipalities would unjustifiably walk away from their

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95. Even though the Supreme Court found the 1934 Act unconstitutional, the Act’s legislative history is relevant to the interpretation of current law. As one treatise explains it, courts look to “prior statutes on the same subject” as a form of interpretation “in pari materia,” often assuming the legislature “must have resorted to the same means to arrive at its purpose.” 2A SINGER & SINGER, supra note 94, § 48:3, at 568–73. In particular, the 1937 Act in effect reenacted the 1934 Act, incorporating a few changes to make clear that the Act did not intrude on state sovereignty, such as excluding counties from eligibility. Compare Act of May 24, 1934, Pub. L. No. 73-251, § 80(a), 48 Stat. 798 (declared unconstitutional in Ashton v. Cameron Cty. Water Improvement Dist., 298 U.S. 513, 532 (1936)) (“[a]ny municipality or other political subdivision of any state” is covered), with Act of Aug. 16, 1937, Pub. L. No. 75-302, § 81, 50 Stat. 653 (listing types of eligible “taxing agencies or instrumentalities” and not including counties). See also The Bankruptcy Reform Act, Revision of the Salary Fixing Procedure for Bankruptcy Judges, Adjustment of Debts of Political Subdivision and Public Agencies and Instrumentalities: Hearings Before the Subcommittee on Improvements in Judicial Machinery of the S. Comm. on the Judiciary, 94th Cong. 210–11 (1975) [hereinafter 1975 Subcommittee Hearings] (statement of Assistant Att’y Gen. Scalia) (comparing Ashton, which held 1934 Act unconstitutional, and Bekins, which held 1937 Act constitutional, and stating, that the “two cases . . . on their facts, do not seem particularly distinguishable”); 6 COLLIER ON BANKRUPTCY, supra note 52, ¶ 900.LH[3], at 900-28 (“The primary differences between Chapter IX [the 1934 Act] and Chapter X [the 1937 Act] were a change in the number of consents needed for confirmation of a plan . . . and a modest increase in the protection of the states’ sovereignty.”); KENNETH N. KLEE, A SHORT HISTORY OF MUNICIPAL BANKRUPTCY 4 (2012), https://cumberland.samford.edu/files/Short%20History%20of%20Municipal%20Bankruptcy.pdf [https://perma.cc/3TAZ-KJ6E] (the 1937 Act “was similar to Chapter IX [the 1934 Act], but leaned slightly more in favor of states’ rights”). The 1937 Act contained the same language relating to insolvency as the 1934 Act. Compare Act of Aug. 16, 1937, § 83(a) (“[t]he Act did not intrude on state sovereignty.”), with Act of May 24, 1934, § 80(a) (same).
debts and a corresponding intention to require that municipalities exhaust their “maximum capacity to pay” before invoking the federal bankruptcy power to reduce their debts.

1. The 1934 Act

Throughout the debate on the 1934 Act, members of Congress called on municipalities to pay all they could toward their debts in bankruptcy. As Senator Matthew Neely of West Virginia argued in opening the Senate floor debate on the bill, the Depression made it “impossible” for many cities to meet obligations because they were “ground by the upper millstone of increasing demands for revenue and the nether millstone of decreasing ability to collect taxes.” The result, he argued, was that “taxing districts [could not] possibly pay their debts according to the letter of the contracts which attest them.”

In light of the Depression, supporters of the Act argued, it was necessary to subordinate debt service to payment for other public services “in order to preserve the communal unit from disintegration.” Under the circumstances of the Great Depression, proponents of municipal bankruptcy argued that their colleagues faced a choice between “orderly refunding” and “chaotic defaults” with no middle way. Municipal bankruptcy was portrayed as being not for cities that had decided their promises were unaffordable or undesirable, but instead for cities that were on the brink of collapse.

As Senator Arthur Vandenberg of Michigan, a principal supporter of the bill, rather lyrically expressed it, the bankruptcy power was to be

96. Statements made in floor debates are relevant to interpreting the Act. Although courts once did not look to statements of individual legislators for help in interpreting statutes, “the traditional view has been modified, and today courts generally do admit statements made by individual legislators during debate to help interpret ambiguous statutes.” 2A SINGER & SINGER, supra note 94, § 48:13, at 613–17. Such statements vary in probative value; statements by a bill’s sponsor, by the “standing committee member charged to present the bill and lead debate,” and statements that “show a common agreement in the legislature about the meaning of an ambiguous provision,” are entitled to greater weight. Id. § 48:13, at 618–19.

97. 78 CONG. REC. 7630, 7641 (1934) (statement of Sen. Neely) (emphasis added); id. at 7642 (“impossible terms” of municipal indebtedness).

98. Id. at 7642 (emphasis added).

99. Id. at 7642 (emphasis added).

100. Id. at 7650 (statement of Sen. Vandenberg); see also id. (noting that bondholders would be harmed by “complete disintegration of the social and communal life in the community,” and giving Detroit as an example, where expenses were cut by forty percent from 1931–1934, in part by discharging 10,000 city employees and “reduce[ing]” the city government “to a survival basis and the employees to a welfare-existence wage”).

101. Id. at 7649.
used to relieve cities on the limited basis that their debts exceeded their maximum “capacity” to pay:

The bill only asks that these groups and units of our fellow citizens shall have an orderly opportunity to survive the concluding phases of this depression, to husband their tax resources against the better day when they may pay their debts in full, to preserve their honor, their credit, and their self-respect, and to protect the rights of those to whom they are indebted, and to whom they intend to pay their debts on the basis of maximum capacity to pay.102

The language of “capacity” came up again when the inevitable question about fairness to creditors arose. Senator Charles Hastings of Delaware asked “whether this is for the relief of the taxpayer, taking it from the bondholder,”103 and Senator Vandenberg replied, “the failure in Michigan cities...to produce an adequate revenue to maintain the full debt service is in no degree due to any unwillingness on the part of the taxpayer to pay and pay and pay to the limit of his capacity.”104 As Vandenberg explained, the bill was in the same spirit as the Canadian system, in which a commission determined the “capacity of the municipality to pay its debts.”105

The debates also seem to assume that taxpayers had obligations respecting municipal debts and to reflect a concern that the bankruptcy power not be used to relieve taxpayers from doing their part to meet municipal obligations. The “decreasing ability to collect taxes” referenced in the debate apparently was not a mere political inability to pass taxes, but instead an economic inability to generate revenue.106

These debates, which took place long before California’s Proposition 13 inaugurated an era of local tax revolt,107 cast doubt on whether the federal bankruptcy power is available to aid a municipality where the taxpayers have disabled local government from raising taxes to pay debts.

102. Id. at 7650 (emphasis added).
103. Id. at 7652 (statement of Sen. Hastings).
104. Id. at 7652 (statement of Sen. Vandenberg) (emphasis added).
105. Id. at 7654.
106. See supra note 98 and accompanying text.
For example, opponents of the statute emphasized the possible negative effects of a municipal bankruptcy statute on the municipal bond market. They also argued that municipal bankruptcy would cause municipalities to make the politically expedient decision to seek bankruptcy protection rather than raise taxes. These arguments were met with the reply that “[t]he people are not able to pay the taxes.” Senator Duncan Fletcher of Florida explained:

The people cannot escape their obligations. They have no desire to repudiate them. There is no inclination to escape the payment of their debts while they are able to pay them and where it is possible for them to pay. They are taxed, however, almost to the limit. In many instances resort has been made to the courts. Any bondholder can go into court and bring suit, where his obligation is in default, and obtain a mandamus to compel the authorities of the municipality, for instance, to levy an assessment. The authorities make the levy. The taxpayers cannot pay the tax.

Members of Congress argued that bankruptcy relief was needed in cities like Pontiac, Michigan, where “[a]s a result of tremendous tax delinquencies” it was “absolutely impossible to maintain . . . debt service” and provide essential services. In response, a pre-Laffer equivalent of the Laffer Curve appeared; cities for which bankruptcy relief is appropriate were those that have passed the point where tax

108. The opponents argued that “it is the duty of the State to come to the relief” of distressed communities “rather than to involve the faith and credit of the tens of thousands of solvent municipalities throughout the entire country.” S. REP. NO. 73-407, at 5 (1934) (statement of minority views); see also 78 CONG. REC. 7656 (statement of Sen. Van Nuys) (Florida municipal insolvencies are “a matter for State relief”).

109. See 78 CONG. REC. 7661 (statement of Sen. Hastings) (asserting that the leaders of a hypothetical town that had borrowed excessively before the depression would “inevitab[ly]” choose to seek bankruptcy protection rather than collecting taxes and that “we are going to see the 2,019 [defaulting municipalities] mount rapidly to 10 times that”); id. at 7663 (“[I]f it were not for the fact that it would result in encouraging cities in the future to disregard their obligations . . . I should be willing to forego my objection to it . . . .”); id. (arguing that in distressed cities such as New York, tax increase opponents would argue for seeking bankruptcy protection). Opponents also argued that states could impose moratoriums on debt payments as another way of getting a breathing space. See id.; id. at 7662 (noting that states could “provide by law that . . . municipalities might declare a moratorium for a certain period, and make it perfectly legal”). Proponents replied that a single uniform federal system was better than forty eight different state systems. Id. (statement of Sen. Vandenberg).

110. Id. at 7663 (statement of Sen. Fletcher) (emphasis added); see also id. at 7739 (statement of Sen. Fletcher) ("[T]he people cannot pay the taxes."); id. at 7740 ("[P]eople cannot pay taxes on the basis of the old value.").

111. Id. at 7739 (emphasis added).

112. Id. at 7651 (statement of Sen. Vandenberg). Vandenberg stated that the city continued to provide essential services, “although on greatly reduced bases.” Id.
increases can generate more revenue. 113

The legislative history also reveals that bankruptcy was intended to benefit, not harm, creditors as a group, despite a background assumption 114 that creditors could compel municipalities to raise taxes outside bankruptcy via mandamus actions, including in federal court. 115

As one supporter argued on the floor of Congress, “there is no existing law under which proceedings of this nature [mandamus actions] can be prevented.” 116 Supporters of the bill argued that the prospect of its passage had increased municipal bond values 117 and that its passage would benefit bondholders still further, 118 despite the creditors’ access to the mandamus remedy. Bankruptcy, then, was intended as a win-win proposition that benefited both debtors as a class and creditors as a class by defeating holdouts who otherwise would obstruct a majority-


114. Legislators’ background assumptions about the law are relevant to interpreting a statute: the “relevant history . . . may include information about . . . contemporary economic conditions, prevailing business practices, and the prior state of the law, including judicial decisions.” 2A Singer & Singer, supra note 95, § 48.4, at 575–77. Such information is relevant if it is “widely available and generally relied upon by the legislators,” id. at 577, that is, reasonably understood as part of legislators’ background assumptions.

115. S. REP. No. 73–407, at 2 (1934) (“These defaulting taxing districts may now be sued by nonresidents in Federal courts as a private person may be sued for debt, and by mandamus may be compelled to levy the necessary tax to meet past due obligations, and their officers may be sent to jail for contempt if they refuse to proceed to the levy and collection of the necessary taxes.”); id. at 4 (municipal bankruptcy bill “proposes to discharge the municipality and its officers from the duty imposed by State law to levy taxes to pay the debts and obligations of the municipality”) (statement of minority views); 78 CONG. REC. 7642 (statement of Sen. Neely) (stating that “[i]n many cases” bondholders’ mandamus proceedings “increase the burdens and add to the embarrassment of the defaulting taxing districts”); id. at 7662 (statement of Sen. King) (recalling that courts had cited local officials for contempt for failing to levy taxes to pay municipal debt); id. at 7739 (statement of Sen. Fletcher) (“The Federal courts already have jurisdiction to issue orders compelling the assessment of taxes.”).


117. Id. at 7654 (statement of Sen. Vandenberg).

118. Id. at 7652; id. at 7654–55 (citing support for bill by insurance companies that held large portfolios of municipal bonds).
approved composition plan.\textsuperscript{119} Congress intended to protect all important classes of creditors; the only losers were to be holdouts who sought to extract more than their fair share from the composition.\textsuperscript{120}

2. \textit{The 1937 Act}

As noted, the 1937 Act made few substantive changes to the 1934 Act, and the debate over the 1937 Act largely reprised the discussion of its predecessor: The bill’s opponents argued that Congress should not aid municipalities in evading their moral obligations,\textsuperscript{121} and the bill’s supporters answered that the bankruptcy bill aided creditors as a group, not just debtor municipalities and their citizens. In particular, the creditors’ remedy outside bankruptcy, a writ of mandamus requiring a tax increase, was ineffective because taxpayers could not or would not pay increased taxes.

For example, the House of Representatives report recognized that creditors of an insolvent municipality could not foreclose, but “must look to the exercise of the taxing power over a period of years,”\textsuperscript{122} and that without intervention of the federal bankruptcy power, the creditors “must resort to mandamus proceedings.”\textsuperscript{123} The report further argued that mandamus proceedings “have not been adequate remedies,” apparently because “the trend of recent decision has been to deny the

\textsuperscript{119} See Act of May 24, 1934, Pub. L. No. 73-251, § 80(a), 48 Stat. 798 (requiring that petition for bankruptcy relief be accompanied by a plan of readjustment accepted by fifty-one of the creditors by value of the taxing district (thirty percent for drainage, irrigation, reclamation, and levee districts)).

\textsuperscript{120} The 1976 Act, with its addition of a “cramdown” provision that permits confirmation of plans that are opposed by a majority of creditors, arguably worked a major change in the purpose of municipal bankruptcy and expanded its purposes far beyond solving the holdout problem. See Kimhi, \textit{Solution in Search of a Problem}, supra note 3, at 366–69. If so, the particular rationale presented in this paragraph might not support considering tax levels in municipal bankruptcy. However, this Article demonstrates that neither the 1976 Act nor its successors deviated from the proposition that tax levels are relevant. See infra Section II.B.

\textsuperscript{121} 81 CONG. REC. 6312 (1937) (statement of Rep. Snell); see also id. at 6319 (statement of Rep. Michener) (stating that investors “relied entirely upon the honesty of the cities and municipalities and the ability of those municipalities to levy taxes to meet the indebtedness . . . . I am opposed to the Federal Government or any other unit of government repudiating its obligations”); id. at 6319 (statement of Rep. Robison) (“I think it is wrong in principle for a government, State, or subdivision of a State to repudiate an honest debt.”); id. at 6320 (statement of Rep. Rees) (“What you are saying is that towns . . . throughout the United States may from now on, if they choose to do so . . . go into court and repudiate their obligations.”); id. at 6323 (statement of Rep. Creal) (“Up until this time the idea of a political unit . . . repudiating a debt has been absolutely foreign to the lay mind in America . . . I want to be in the Record as in opposition to it.”).

\textsuperscript{122} H.R. REP. NO. 75-517, at 3 (1937); see also S. REP. NO. 75-911, at 2 (1937).

\textsuperscript{123} H.R. REP. NO. 75-517, at 3; see also S. REP. NO. 75-911, at 2.
writ of mandamus wherever sound judicial discretion justifies denial." Thus, “creditors have been unable to obtain unjust advantage, but the problem of the municipality or taxing district has remained unsolved,” so that the bankruptcy bill “remove[s] an apparent impasse.”

Similar points came up in the floor debate on the bill. When Representative Bertrand Snell of New York argued that the bankruptcy bill would permit municipalities where “[t]he moral responsibility of the community is not very strong” to “repudiate and beat the honest holders of . . . securities out of their money,” the answer, delivered by William Driver of Arkansas, was that composition benefited creditors because “[t]he taxpayers of the district find themselves unable to meet that great amount of debt.” The key selling point was that creditors are aided when a composition “bring[s] the total of amounts payable within the ability of the debtor to pay.” Notably, the focus was on the taxpayers’ ability to pay, that is, whether additional taxes would in fact raise revenue.

Representative Hatton Sumners, Democrat of Texas, responded to Snell’s objection in similar terms, using “the ability of the municipality to collect taxes” as the yardstick.

124. H.R. REP. NO. 75-517, at 3; see also S. REP. NO. 75-911, at 2–3. Representative Wilcox of Florida, one of the bill’s major proponents and the author of the 1934 legislation, argued that “the court has no discretion” in granting mandamus to support bondholders’ actions, so holdout bondholders had too much leverage in resisting, and therefore undoing, compositions. 81 CONG. REC. 6316.

125. H.R. REP. NO. 75-517, at 3; see also S. REP. NO. 75-911, at 2–3.


127. Id. at 6313 (statement of Rep. Sumners) (emphasis added); see also id. (“Whatever may be the theory with regard to the ability of creditors to force these municipalities to pay, it does not work . . . . There is no effective government agency that can compel a municipality to pay its bonds.”). Representative Wilcox observed that the mandamus remedy was “entirely impractical” because “[a] tax levy can be put on, but nobody as yet has devised a means of reaching down into the pockets of the taxpayers and making them pay a tax which they think is inequitable and unfair.” Id. Wilcox appears to be discussing tax burdens that are not just unfair, but also uneconomic:

Of course, you can sell his property under a tax execution or under some other means of foreclosing the tax; but, after all, the man who buys the property at the tax sale buys it subject to the whole debt again, and he, in turn, can lose it next year on the same thing.

Id.

128. The full exchange reads as follows:

Mr. Snell. I do not want to pass any legislation that will make it easier for some of these communities which do not fully appreciate the moral responsibility which rests upon that community to repudiate some of their debts . . . .

Mr. Sumners of Texas. Finally, you reach a situation in the case of some of these municipalities where the bonded indebtedness is greater than the ability of the municipality to collect taxes to retire the indebtedness. I think this is absolutely true with reference to many of these municipalities. This legislation, as we see it, is in favor of the people who own these bonds . . . .

Mr. Snell. We know that in some of these communities there are always some people saying
Other representatives were even more direct in expressing that municipalities were supposed to impose taxes to pay debts, at least up to the practical limits of the ability to collect. Representative Sam Hobbs, Democrat of Alabama, indicated that the bankrupt municipality’s taxing power would be subject “wholly and unreservedly” to the bankruptcy court, which would be bound to “safeguard to the uttermost the ‘interests of the creditors.’” 129 At the same time, Hobbs expressed the idea of the Laffer Curve some forty years before Wanniski popularized the term. Hobbs recognized that the bankruptcy court’s ability to protect creditors was limited by the fact that “the power to tax . . . frequently cannot collect.” 130 More colorfully, Hobbs explained that “by taxation which is unreasonably high you can . . . kill a goose which, while not laying, might, under revised conditions, resume that happy function.” 131

Just as in the debate over the 1934 Act, supporters argued that the standard for invoking bankruptcy protection was high. Senator William Dieterich of Illinois reaffirmed that municipalities were expected to pay “as much as they can pay without destroying the taxing body or the municipality.” 132

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129. Id. at 6321 (statement of Rep. Hobbs).
130. Id.
131. Id. (“The truth of the old adage ‘You cannot get blood from a turnip,’ was never better illustrated than by those within the six classes of petitioners described in this bill. All they have is their taxing power. Seldom, if ever — and then only after foreclosure — have they any property. All they can bring into court is their taxing power. This they do and subject it and themselves wholly and unreservedly to the jurisdiction and sound discretion of a court of equity. That court is bound by the terms of the bill to safeguard to the uttermost the ‘interests of the creditors.’ The power to tax has been held to be the power to destroy . . . . But the power to tax, while it may destroy, frequently cannot collect. You may kill the goose that lays the golden eggs, and by taxation which is unreasonably high you can also kill a goose which, while not laying, might, under revised conditions, resume that happy function.”).
132. Id. at 8544 (statement of Sen. Dieterich); id. at 8545–46 (statement of Sen. Pepper) (special districts seeking bankruptcy protection may not have property to surrender, but “[t]hey must surrender all they have. In the case of municipalities . . . it is in the discretion of the Federal court . . . to make full investigation and to determine whether or not the petitioning debtor has made a full and fair disclosure of its ability to pay”). Dieterich was responding to concerns about municipal opportunism that were phrased in very similar terms to those Representative Snell used. See id. at 8544 (statement of Sen. King) (arguing that if bankruptcy bill passed, “there will not be an invitation for [eligible] municipalities to exercise the taxing power which they have or to resort to other measures for defending the prestige and honor and credit of the municipality” but would seek
Although the idea that municipalities and their taxpayers should pay as much as possible toward their debts was often invoked as a general background principle of the bill, it also came up in connection with specific provisions. The bill’s supporters stressed that the insolvency requirement—the requirement that the municipality be unable to meet obligations before seeking bankruptcy relief—was part of the solution to the problem of opportunistic bankruptcy. Shortly after the exchange quoted above, Sumners explained that as a prerequisite of relief, “[t]he court must first ascertain that [the petitioning municipality is] in a condition where [it] cannot pay [its] indebtedness.” Representative J. Mark Wilcox of Florida likewise answered the concern about debt repudiation by “call[ing] attention” to the provision providing that “[t]he Federal judge to whom this petition for confirmation must be submitted must find, first of all, that the taxing district is insolvent or unable to meet its debts as they mature.”

The requirement that the composition be in the “best interests of the creditors” also reflects the view that municipalities should pay all they can toward their debts. Representative Wilcox explained that test as follows:

[T]he judge is charged with the responsibility of seeing to it that the creditor is protected. Not only that it is a fair settlement, not only that it is just and equitable, not only that it represents the full capacity of the community to pay, but he must find that it is in the interest of the creditor — not that the municipality has not put over something on the creditor, but that it is in the interest of the creditor; and then it goes further and puts this responsibility on the judge, and this protects the unrepresented creditor from the represented creditor before the court.

3. The 1946 Act

The next significant legislative discussion of municipal bankruptcy came in 1946, when Congress made the municipal bankruptcy chapter permanent. Again, appropriate use of municipal bankruptcy was
reduction of debts to what a municipality reasonably could pay. As one experienced bond lawyer told the House Judiciary Committee, “I have seen the proceedings of more than 100 cases, possibly 150, in which the various drainage and irrigation districts reduced the indebtedness to where they could pay, and I have never yet seen an abuse by this act or under this act.”


Although the 1976 Act marked a comprehensive change in municipal bankruptcy, aimed at making the procedure useful to larger cities, there was no change in congressional intention that municipalities try to pay their debts, including trying to pay through raising revenue. If anything, the language calling for use of the taxing power became even more explicit in the period that started with the 1976 Act; moreover, Congress expressly directed courts to take guidance from cases under the previously existing statutes that required tax increases.

**1. The 1976 Act**

Although the 1976 Act comprehensively revised municipal bankruptcy, the legislative history seems to have little to say about taxes specifically. But what it does have to say is emphatic. The House report on the 1976 Act expressly states that “[t]he petitioner must exercise its taxing power to the fullest extent possible for the benefit of its creditors.”

The report supports its proposition by citing Kelley v. Everglades Drainage District and Fano v. Newport Heights Irrigation District, leading cases for the proposition that municipalities must, in appropriate situations, meet debt obligations using tax revenues.

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140. H.R. REP. NO. 94-686, at 33 (1975) (citing Fano v. Newport Heights Irrigation Dist., 144 F.2d 563 (9th Cir. 1940)); see also id. at 32–33 (stating that plan feasibility is to be determined based on likelihood of tax collection (citing Kelley v. Everglades Drainage Dist., 319 U.S. 415 (1943))). The Report also states that the “fair and equitable” test “incorporates the absolute priority rule . . . which requires that senior creditors be paid in full before any creditor junior to them may be paid at all. The court determines these priorities based on State law.” *Id.* This statement appears relevant to state efforts to give priority to pension claims, a subject generally beyond the scope of this Article.

141. 319 U.S. 415 (1943).

142. 144 F.2d 563 (9th Cir. 1940).

143. See *infra* Section III.C.
Kelley and Fano were also endorsed by then-Assistant Attorney General Antonin Scalia, who testified in support of the Ford Administration’s proposal for a new bankruptcy statute limited to “major municipalities,” such as New York City.\textsuperscript{144} Scalia cited Kelley in arguing that the valuation of creditors’ claims “would require a considered estimate based on a proper factual foundation of the estimated revenues of the municipality.”\textsuperscript{145} The “estimated revenues” were to include not just what the municipality would bring in without adjusting course, but also money that the municipality could lay its hands on by taking unusual measures: in determining the estimated revenues, “[c]onsideration would . . . have to be given to non-income producing assets of the municipality which could appropriately be made to yield income or which, if currently not used, could be sold.”\textsuperscript{146} Although the Ford Administration’s proposal was not adopted, Scalia’s statement indicates that the administration accepted that municipal bankruptcy relief required the city to go outside the normal course of business to acquire funds.

2. The 1978 Act

Kelley and Fano reappeared in the legislative history of the 1978 Act, this time in connection with the “best interests of the creditors” test, which the 1978 Act reintroduced as a separate requirement for cram down plan confirmation in municipal bankruptcy, distinct from the “fair and equitable” test.\textsuperscript{147}

The 1978 Act was a comprehensive reform of bankruptcy law that touched on many subjects other than municipal bankruptcy, and its sponsors discussed taxes as part of their explanation of how the various parts of the Act fit together. At the same time that the 1978 Act revived the term “best interests” for municipal bankruptcy,\textsuperscript{148} it adopted a more precise version of the test for use in corporate reorganizations, requiring that a corporate reorganization plan provide each creditor with as much

\textsuperscript{144} 1975 Subcommittee Hearings, supra note 95, at 197–228 (testimony of Assistant Att’y Gen. Scalia).
\textsuperscript{145} Id. at 204.
\textsuperscript{146} Id.
\textsuperscript{147} The Senate bill, S. 2266, would not have revived the “best interests” requirement and would have required only that the plan be fair and equitable and feasible. S. 2266, 95th Cong. § 101 (1978) (provision that was to be codified at 11 U.S.C. § 946(b)(1) (2012)).
\textsuperscript{148} See H.R. Rep. No. 95-595, at 400 (1977) (explaining that “best interest” test had previously been deleted from municipal bankruptcy statute because it was “redundant with the fair and equitable rule” but was being restored as a separate test in the 1978 Act).
value as that creditor would have received in a liquidation of the debtor.\textsuperscript{149} Supporters of the Act distinguished between municipal and corporate bankruptcy by arguing that liquidation value did not make sense as a benchmark in municipal bankruptcy.\textsuperscript{150} In elaborating on what “best interests” did mean in municipal bankruptcy, the House and Senate sponsors of the 1978 Act explained:

The best interest of creditors test does not mean liquidation value as under Chapter XI of the Bankruptcy Act. In making such a determination, it is expected that the court will be guided by standards set forth in Kelley v. Everglades Drainage District, 319 U.S. 415 (1943), and Fano v. Newport Heights Irrigation Dist., 114 F.2d 563 (9th Cir. 1940), as under present law, the bankruptcy court should make findings as detailed as possible to support a conclusion that this test has been met.\textsuperscript{151}

The Senate version of the 1978 Act, which would have left “best interests” as part of the “fair and equitable” requirement, explained:

Creditors must be provided, under the plan, the going concern value of their claims. The going concern value contemplates a ‘comparison of revenues and expenditures taking into account the taxing power and the extent to which tax increases are both necessary and feasible’ and is intended to provide more of a return to creditors than the liquidation value if the city’s assets could be liquidated like those of a private corporation.\textsuperscript{152}

Edwards’ and DeConcini’s statement about the importance of Kelley and Fano has not escaped the attention of other scholars.\textsuperscript{153} Their

\textsuperscript{149} See 11 U.S.C. § 1129(a)(7)(A)(ii); H.R. REP. NO. 95-595, at 400; 7 COLLIER ON BANKRUPTCY, supra note 5252, ¶ 1129.02[7], at 1129-33 (referring to 1129(a)(7) as the “best interests of creditors” test).

\textsuperscript{150} The House Judiciary Committee report on H.R. 8200 observed that in the context of a corporate reorganization, the requirement “is phrased in terms of the liquidation of the debtor” and noted that “[b]ecause that is not possible in a municipal case, the test here is phrased in its more traditional form, using the words of art ‘best interests of creditors.’ The best interest of creditors test here is in addition to the financial standards imposed on the plan” under the provisions of Section 1129 that are incorporated by reference. H.R. REP. NO. 95-595, at 400.


\textsuperscript{152} S. REP. NO. 95-989, at 113 (1978) (quoting Lawrence P. King, Municipal Insolvency: Chapter IX, Old and New; Chapter IX Rules, 50 AM. BANKR. L.J. 55, 64 (1976)). Although Congress adopted the House version of the bill and reestablished the “best interests” test as a requirement separate from “fair and equitable,” there is no indication that the chambers differed in their understanding of what best interests required.

\textsuperscript{153} See, e.g., McConnell & Picker, supra note 3, at 465 n.178 (quoting Rep. Edwards’ statement); Kordana, supra note 90, at 1060–61 (same).
explanation takes on even greater significance than may have been previously appreciated, however, when evaluated in context. Just three years before, the 1976 Act committee report had indicated that Kelley and Fano stood for the proposition that municipality was to exercise its taxing power “to the fullest extent possible” for the benefit of creditors. Moreover, as demonstrated, the sponsors’ reference to the cases is part of a history of insistence on taxes as part of the price of municipal bankruptcy relief that goes back to the 1930s, and is in agreement with a Senate bill that provided a similar standard.

3. The 1988 Act

The most important aspect of the 1988 Act for this Article is its adoption of the special definition of insolvency for the bankrupt municipality: “generally not paying its [ undisputed ] debts as they become due” or “unable to pay its debts as they become due.”

154. See H.R. REP. NO. 94-686, at 33 (1975) (citing Fano v. Newport Heights Irrigation Dist., 144 F.2d 563 (9th Cir. 1940)); see also id. at 32–33 (citing Kelley v. Everglades Drainage Dist., 319 U.S. 415 (1943)).


156. Congress recognized that the ordinary definition of insolvency, comparing nonexempt assets to liabilities, “does not work when applied to a municipality because . . . most of the assets of a municipality are not subject to creditors’ claims in the first place.” See 1988 Hearings, supra note 155, at 533 (statement of Lawrence P. King, Professor, New York University School of Law); id. at 546; Report of the National Bankruptcy Conference on Proposed Municipal Bankruptcy Amendments, supra note 155, at 546 (under balance sheet test, “virtually every municipality . . . is insolvent”); also noting that even if municipality’s assets could be seized to pay debts, the assets are probably “so tailored to a specific purpose that their value is uncertain at best.”); 133 CONG. REC. 31822 (1987) (statement of Sen. DeConcini) (same); S. REP. NO. 100-506, at 10 (1988) (same, adding “the value of city hall should make little difference to creditors”); id. at 24 (statement of Department of Justice views) (“many municipal assets (such as roads) have market values which are speculative at best”); H.R. REP. NO. 100-1011, at 5–6 (1988) (“What is important to creditors is not the value of the municipality’s assets, but rather the ability of the municipality to pay its debts.”); 1988 Hearings, supra note 155, at 559 (“Many municipal assets are special-purpose assets and have a highly uncertain market value, which is probably less than cost. Under these circumstances, many healthy municipalities would be treated as ‘insolvent’. Also many municipal assets cannot be reached to pay debts, rendering the assets vs. liabilities test somewhat irrelevant to creditors.”); id. at 655 (letter from Lawrence P. King, Professor, New York University School of Law to the Hon. Dennis DeConcini, June 24, 1988) (same).


158. Id. § 101(32)(C)(ii). By contrast, entities other than municipalities are insolvent, loosely
Although the legislative history of the 1988 Act does not mention taxation, it does reflect a concern with bona fide, legitimate insolvency: “financially sound” municipalities would not qualify as insolvent, and the test would focus on “the ability of the municipality to pay its debts.”

Congress did not intend that municipalities would be able to invoke bankruptcy protection by engineering a technical insolvency. As the Report of the National Bankruptcy Conference on the Act stated, “[a] deliberate failure to pay indebtedness in order to create eligibility to file a petition under this chapter would be grounds for dismissal under section 921(c) as failure to file in good faith.” The legislative history of municipal bankruptcy from the 1976 Act indicates that Congress intended, as the 1976 Act House report states, that the bankrupt municipality “exercise its taxing power to the fullest extent possible for the benefit of its creditors.” The report indicates that Kelley and Fano support that conclusion—a view with which the Ford Administration concurred through the testimony of Assistant Attorney General Scalia. Three years after the report, the House and Senate sponsors of the 1978 Act expressly stated that they expected the courts to be guided by Kelley and Fano. Thus, both major bankruptcy statutes from this era reflect an expansive view of the municipality’s duty to tax. The 1988 Act did not disturb this view; indeed, the House report’s concern with bona fide, legitimate insolvency reinforces the view that bankrupt municipalities are to make strenuous efforts to meet their obligations.

speaking, when the fair value of nonexempt assets is less than liabilities. Id. § 101(32)(A). The definition of insolvency also excludes assets that have been fraudulently transferred away from the potentially insolvent entity. Id. § 101(32)(A)(i). There is also a special definition for partnership insolvency, but it is based on comparing assets and liabilities. Id. § 101(32)(B).


162. See H.R. REP. NO. 94-686, at 33 (1975) (citing Fano v. Newport Heights Irrigation Dist., 144 F.2d 563 (9th Cir. 1940)).
III. TAXES AND MUNICIPAL BANKRUPTCY: JUDICIAL AUTHORITY

The legislative history of the municipal bankruptcy statutes reflects a general principle that a municipal population’s unwillingness to tax itself to pay for benefits received is relevant to the municipality’s eligibility for federal bankruptcy relief. Although this assumption sometimes was articulated in connection with particular provisions of the Code, it was just as commonly stated as a general background assumption of the bankruptcy statute.

This Part focuses on how the taxes-are-relevant principle has appeared in cases applying four specific provisions of the Code: the insolvency and good-faith requirements for eligibility and the “best interests” and “fair and equitable” tests for plan confirmation. The Part demonstrates that courts and commentators have recognized that tax levels are relevant both to eligibility for municipal bankruptcy and to plan confirmation under these four statutory provisions.

Although much of the authority embracing the principle is older and deals with smaller municipalities and special-purpose districts, taxes most definitely were found relevant in the recent bankruptcies of larger general-purpose municipalities. The written opinions in the Detroit case, in which the plan did not raise taxes, suggest that the judge found that the city had been taxed to the point where further tax increases would not produce any revenue. In the Stockton case, the court relied expressly on the fact that the plan was going to propose a tax increase as a reason for finding the city eligible for bankruptcy and relied on the fact that the voters passed an increase in confirming the plan.

163. Clayton Gillette has identified three of these four provisions: insolvency, good faith negotiations, and best interests of creditors. Gillette, Fiscal Federalism, supra note 46, at 293–96. This Article identifies additional precedents and discussing the authorities in greater detail in the course of making a different argument about municipal taxes.

164. Taxes also are relevant to the requirement that a plan be “feasible,” 11 U.S.C. § 943(b)(7) (2012), and the related requirement that the plan provide “adequate means for [its] implementation,” id. § 901(a) (incorporating 11 U.S.C. § 1123(a)(5) into Chapter 9); see also Reporter’s Transcript of Proceedings: Findings of Fact and Conclusions of Law 33–34, In re City of Stockton, 493 B.R. 772, (Bankr. E.D. Cal. 2014) (No. 12-32118-C-9) [hereinafter Stockton Transcript] (evaluating tax levels in connection with finding that plan of adjustment had adequate means for its implementation). However, these provisions address an aspect of municipal bankruptcy that is not the main concern of this Article. They address whether the city will be able to make the payments its plan proposes. Id. The more debts are cut, the more feasible a plan becomes. This Article focuses on the constraints that apply to the decision to cut debts in the first place.
A. The Insolvency Requirement: Unable, Not Unwilling

Chapter 9 requires that a debtor be insolvent as a condition of filing for relief. Insolvency means that the debtor is “generally not paying its debts as they become due” or is “unable to pay its debts as they become due.” Demonstrating insolvency under the Code requires something more than showing that the debtor is in financial trouble, but exactly what that “something more” is has proven more difficult to define.

General-purpose municipalities typically have filed under Chapter 9 before actually running out of cash and therefore have tended to rely on the “unable to pay” branch of the insolvency test. This provision, as phrased, would seem to confer upon the court the discretion to decide that a municipality is “able to pay” if taxes could provide the revenue needed to meet obligations. However, no court has gone so far as to say exactly that, although municipalities have been found insolvent if they could take other unusual measures, such as issuing warrants, to get cash. Moreover, one articulation of the “unable to pay” standard, the

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166. 11 U.S.C. § 101(32)(C)(i). Failure to pay a single debt, for example, does not establish that the municipality is “generally” failing to pay debts when due. Boise Cty., 465 B.R. at 171.

167. 11 U.S.C. § 101(32)(C)(ii). The 1988 Act added this definition of insolvency. Act of Nov. 3, 1988, Pub. L. No. 100-597, § 1, 102 Stat. 3028, 3028. Previously, the Code had provided that a municipality must be “insolvent or unable to meet such entity’s debts as such debts mature” to seek bankruptcy protection, Act of Nov. 6, 1978, Pub. L. No. 95-598, § 109, 92 Stat. 2549, 2557, and municipalities were subject to the general definition of insolvency: that the entity’s debts were greater than the fair value of the entity’s nonexempt property. 11 U.S.C. § 101(26)(A). The change reflects the general perception that municipal property cannot be levied on to satisfy the municipality’s creditors. See H.R. REP. No. 95-595, at 263 (1977); 6 COLLIER ON BANKRUPTCY, supra note 52, ¶ 900.02[c], at 900-21.

168. See In re City of Bridgeport, 129 B.R. 328, 336 (Bankr. D. Conn. 1991) (“[T]he issue is not whether Bridgeport was in financial trouble, but rather whether it was insolvent when it filed.”); In re Hamilton County Metro. Dist., 143 F.3d 1381, 1386 (10th Cir. 1998) (“[T]he inability to pay under § 101(32)(C)(ii) ‘depend[s] upon the inescapable quality of the obligation and the certainty that it cannot be met. Mere possibility or even speculative probability is not enough.’” (quoting In re Town of Westlake, 211 B.R. 860, 865 (Bankr. N.D. Tex. 1997))).

169. See Stockton, 493 B.R. at 787 (“[T]he issue is not whether Bridgeport was on the second prong of the municipal insolvency definition.”); In re City of Vallejo, No. 08-26813-A-9, 2008 WL 4180008, at *22 (Bankr. E.D. Cal. Sept. 5, 2008) (“[T]he City must demonstrate that . . . it will be unable to pay debts as they become due.”); City of Bridgeport, 129 B.R. at 334 (“The issue here is whether Bridgeport was ‘unable to pay its debts as they become due.’”). Detroit is a notable exception: it was both unable to pay its debts and not paying its debts when it filed. In re City of Detroit, 504 B.R. 97, 168 (Bankr. E.D. Mich. 2013) (“The Court finds that the City . . . is . . . insolvent under both definitions.”).

170. In Boise County, the court found that the debtor county was not insolvent because the
cash-flow test, focuses on whether it is “imminent and certain”\textsuperscript{171} that the municipality will run out of money to pay its debts. The cash-flow test on its face seems to look to whether the city will run out of money, not to whether it could avoid running out by raising taxes.\textsuperscript{172}

Nevertheless, courts frequently suggest that the ability to raise taxes is relevant to the municipality’s insolvency. Many insolvency decisions rely on findings that raising taxes would be revenue-decreasing\textsuperscript{173} or legally impermissible\textsuperscript{174} rather than on a proposition that the ability to raise taxes does not matter in evaluating insolvency.\textsuperscript{175}
In particular, the recent major cases of Stockton and Detroit both demanded “bona fide financial distress,” as distinguished from a “technical” or “engineered” insolvency, and both decisions found taxes relevant. Both cases treated the city’s ability to extricate itself from financial distress by raising taxes as relevant to whether the municipality faces bona fide insolvency.

In re City of Stockton stressed the importance of good-faith insolvency and found taxes relevant to the city’s good faith. The court started with the proposition that “the municipality must be in bona fide financial distress that is not likely to be resolved with use of the federal exclusive bankruptcy power to impair contracts.” Accordingly, the court found Stockton was cash-flow insolvent, but did not stop there: cash-flow insolvency was not enough. The court went on to evaluate the claim of capital market objectors that the insolvency was “engineered and not genuine.” In so doing, the court considered two other concepts of insolvency, “service delivery insolvency” and “budget insolvency.”

Service delivery insolvency indicates the city’s inability to “pay for all the costs of providing services at the level and quality required for the health, safety, and welfare of the community.” Noting that Stockton’s police department had been “decimated,” that crime had “soared,” and “homicides [were] at record levels,” with police “often respond[ing] only to crimes-in-progress,” the court concluded that the city was a “paradigm example of service delivery insolvency.” This finding in turn bolstered the ultimate conclusion—that Stockton was insolvent in

24 B.R. 632, 639 n.6 (Bankr. M.D. Tenn. 1982). It is difficult to know what to make of this decision, which has been cited only once for its tax-related holding, in In re Sullivan Cty. Reg’l Refuse Disposal Dist., 165 B.R. 60, 78 (Bankr. D.N.H. 1994) (“[D]ebtors coming into the bankruptcy courts under Chapter 9 do not have to demonstrate that they have fully exercised their taxing powers to the maximum extent possible.”). Sullivan County, in which the court held that the debtor was ineligible for Chapter 9 because it did not file its petition in good faith, is discussed in more detail infra Section III.B.


177. Stockton, 493 B.R. at 791.

178. Id. at 789.

179. Id. at 772.

180. Id. at 788.

181. Id. at 789.

182. Id.

183. Id. at 781.

184. Id.

185. Id. at 789–90.

186. Id. at 790.
good faith: “[t]hat [Stockton] was service delivery insolvent confirms that the cash insolvency was not a mere technical insolvency.” 187 The court also found that the city was “budget insolvent,” meaning that it was not able to “create a balanced budget that provides sufficient revenues to pay for its expenses that occur within the budgeted period,” including future years. 188 This finding likewise supported the conclusion that Stockton’s insolvency was genuine. 189

The Stockton court treated taxes as relevant to the question of bona fide insolvency. 190 The court directly addressed the capital-market creditors’ argument that the city should have tried to raise taxes before filing for bankruptcy and credited testimony that it would have been futile to seek a pre-bankruptcy tax increase because voters would not have approved it. 191

The Detroit opinion quoted Stockton when it affirmed the requirement of “bona fide financial distress.” 192 Although Detroit was not as explicit as Stockton in considering taxes in determining good-faith insolvency, the decision did evaluate insolvency against a background finding that “[t]he City cannot legally increase its tax revenues.” 193 If Detroit had been able to raise more money by increasing taxes, the finding of insolvency could—and likely would—have been different.

Stockton and Detroit were not the first opinions to stress bona fide insolvency and to find a connection between that concept and the legal or practical ability to raise revenues through taxing. For example, a bankruptcy court found that the town of Westlake, Texas was not insolvent because it had options short of bankruptcy available to it for paying its debts. 194 The court held that the Bankruptcy Code’s insolvency test “does not appear to encompass a situation where a municipality deliberately budgets or spends itself into insolvency . . . when other realistic avenues and scenarios are possible.” 195 Although the court did not go so far as to say that the city

187. Id. at 791.
188. Id. at 790.
189. Id. at 791 (“[I]nsolvency would persist without realignment of revenues and expenses.”).
190. Id. at 790.
191. Id.
193. Id. at 121.
194. In re Town of Westlake, 211 B.R. 860, 866–67 (Bankr. N.D. Tex. 1997) (noting unnecessary and unusual expenditures in the town budget and the town’s untapped ability to raise taxes as reasons for finding that “there was insufficient credible proof that Westlake is unable to pay its debts as they come due”).
195. Id. at 867; see also 2 COLLIER ON BANKRUPTCY, supra note 52, ¶109.04[3][d][iii], at 109-30
could have avoided bankruptcy by raising taxes, the court did mention the city’s untapped ability to impose an ad valorem tax in the course of deciding the city was not insolvent.\textsuperscript{196}

California requires electoral approval of most new taxes,\textsuperscript{197} and it is worth specifically emphasizing how bankruptcy courts in California have treated this requirement in their insolvency opinions. The courts in the recent major California general municipal bankruptcies in which insolvency was litigated, those of Vallejo and Stockton,\textsuperscript{198} have not pushed back against California’s electoral-approval requirement.\textsuperscript{199} Both courts rejected arguments that the city was not insolvent because it could raise taxes, basing the conclusion at least in part on the proposition that the voters would not approve the suggested tax increases. In \textit{Stockton}, for example, the court rejected the capital market creditors’ argument that the city was solvent because it did not “go to the people for a tax increase before filing a chapter 9 case.”\textsuperscript{200} The court credited testimony from Stockton’s city manager that the voters probably would have rejected a tax increase.\textsuperscript{201}

The cases therefore could be understood to stand for the proposition that a city may be insolvent in good faith if city voters would refuse to approve taxes to meet municipal obligations, no matter what the city’s ability to pay or current tax level.\textsuperscript{202} But such an understanding is

\begin{quote}
("A municipality cannot deliberately budget or spend itself into insolvency when other scenarios are possible.").
\end{quote}

\textsuperscript{196} \textit{Town of Westlake}, 211 B.R. at 867. \textit{Town of Westlake} involved unusual facts. The town’s reason for seeking bankruptcy protection may have been to get access to the bankruptcy court’s avoidance powers to reverse the contested disannexation of a business park rather than to adjust debts. \textit{Id.} at 862–63. Moreover, the city’s budget, adopted immediately before the hearing to dismiss the bankruptcy petition, included major unexplained increases in expenses from prior years. \textit{Id.} at 866.

\textsuperscript{197} \textit{In re City of Stockton}, 493 B.R. 772, 790 (Bankr. E.D. Cal. 2013) (assuming that a tax increase sufficient to affect city’s insolvency would require electoral approval).

\textsuperscript{198} An objection to insolvency in the San Bernardino case was withdrawn. See, e.g., \textit{In re City of San Bernardino}, 499 B.R. 776, 781 (Bankr. C.D. Cal. 2013) (noting that an employee association withdrew its objection to city’s claim of insolvency).

\textsuperscript{199} It might be argued, for example, that applying electoral approval requirements for taxes to a bankrupt municipality impermissibly invades the federal bankruptcy power and therefore is not protected by section 903 of the Bankruptcy Code, which preserves state control of municipal political and governmental authority in bankruptcy. \textit{Cf. City of Stockton}, 526 B.R. at 37 (finding that California law prohibiting municipality’s rejection of a CalPERS pension servicing contract in bankruptcy amounts to “usurp[ing] the exclusive power of Congress to legislate uniform laws on the subject of bankruptcy”).

\textsuperscript{200} \textit{Stockton}, 493 B.R. at 790.

\textsuperscript{201} \textit{Id.}

\textsuperscript{202} At least one other court seems to have rejected that argument. See \textit{In re Ellicott School Bldg. Auth.}, 150 B.R. 261, 265 (Bankr. D. Colo. 1992) (“It is clear that the School District’s taxpayers
incomplete. In *Stockton*, the court did not find that the population had no responsibility to raise taxes; by contrast, its insolvency opinion makes clear that bankruptcy was itself a way of getting to a settlement that included taxes. As the court put it, “the extra revenues needed to fund a plan of adjustment probably will have to come from tax increases,” and bankruptcy was a vehicle for passing such increases:

>[S]uccessful local tax measures for general-purpose revenues occur in an atmosphere in which the predicate message is that the fiscal house is already in order. Putting the fiscal house in order so that voters might be willing to entreat tax increases is the whole point of chapter 9.\(^{204}\)

As it turned out, the court was right; the bankruptcy plan was in fact the vehicle for a successful tax-increase campaign in Stockton.\(^{205}\)

In *Vallejo*, the court found the city insolvent despite an objector’s claim that Vallejo should have tried to increase taxes. The court’s decision was based in part on the city’s argument that a tax increase would not pass muster with the voters.\(^{206}\) But the court had numerous independent grounds for its finding of insolvency, including that it did not find the objectors’ expert credible,\(^{207}\) that the objectors’ expert did not in fact conclude that the city was not insolvent,\(^{208}\) and that objectors’ counsel admitted that efforts to avoid bankruptcy by enhancing revenue were unlikely to work for reasons other than the difficulty of getting electoral approval.\(^{209}\) Moreover, the ultimate outcome in Vallejo was a tax increase\(^{210}\) that the voters approved,\(^{211}\) so it is difficult to make the

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\(^{203}\) Stockton, 493 B.R. at 790.

\(^{204}\) Id.

\(^{205}\) See infra Section III.C.

\(^{206}\) In re City of Vallejo, No. 08-26813-A-9, 2008 WL 4180008, at *17 (Bankr. E.D. Cal. Sept. 5, 2008) (“[I]n the current economic and political environment, the City reasonably believes that voter approval of any additional taxes and assessments is unlikely.”).

\(^{207}\) Id. at *16 (noting that an expert damaged his credibility by initially declining the assignment, then reversing himself and taking it after determining that the city’s bankruptcy case would harm his other clients).

\(^{208}\) Id. at *17 (“The basic problem with [the expert’s] report and testimony was that he did not conclude that the City was not insolvent.”).

\(^{209}\) Id.


\(^{211}\) See Rachel Raskin-Zrihen, *New Vallejo Sales Tax Rates Begin April 1, Rise to 8.375
case stand for the proposition that taxes are irrelevant in municipal bankruptcy.

B. The Good Faith Requirement: Bankruptcy’s Intended Purpose

The Detroit and Stockton courts found good faith relevant to insolvency. But good faith is more than that; it is also an explicit requirement for filing, and courts occasionally have emphasized a distinction between insolvency and good faith. The court may dismiss a Chapter 9 case at any time if the petition is not filed in good faith, and courts have taken the municipality’s taxing power into account in deciding whether to exercise this discretion.

The good-faith requirement is an appropriate statutory provision through which to apply the principle that taxes are relevant. The idea that municipalities should not walk away from debts they can afford to pay appears throughout the legislative history of municipal bankruptcy, as shown in Part III, but is not clearly encapsulated in so many words in any provision of the Code. The good-faith rule captures such situations. In the words of one court: “[t]he primary function of the good faith requirement has always been to ensure the integrity of the reorganization process by limiting access to its protection to those situations for which


212. See, e.g., In re Sullivan Cty. Reg’l Refuse Disp. Dist., 165 B.R. 60, 75–76 (Bankr. D.N.H. 1994) (holding that the district’s failure to levy a special assessment is relevant to district’s eligibility for bankruptcy, but under the heading of good faith rather than that of insolvency); In re McCurtain Mun. Auth., No. 07-80363, 2007 WL 4287604, at *4 (Bankr. E.D. Okla. Dec. 4, 2007) (“[T]he failure to impose assessments, if relevant at all, concerns ‘good faith’ issues, not a Debtor’s insolvency status.”).

213. 11 U.S.C. § 921(c) (2012); see also 1988 Hearings, supra note 155, at 560 (Report of the National Bankruptcy Conference on Proposed Municipal Bankruptcy Amendments) (“A deliberate failure to pay indebtedness in order to create eligibility to file a petition under this chapter would be grounds for dismissal . . . [for] failure to file in good faith.”). Other provisions of Chapter 9 require good faith but are not discussed here: The debtor must “negotiate[] in good faith with creditors” and “fail[] to obtain” their agreement as a condition of filing the Chapter 9 petition unless the debtor has obtained the agreement of a majority of impaired creditors, reasonably believes that a creditor may seek an avoidable transfer, or can show that negotiation with creditors is impracticable. 11 U.S.C. § 109(c)(5)(B)–(D); see also H.R. REP. No. 94-938, at 17 (1976) (Conf. Rep.) (explaining that the negotiation-related requirement’s “purpose . . . is to limit accessibility to the bankruptcy court somewhat, as does current law, without making the accessibility requirement so stringent as to preclude relief in a situation in which the petitioner is confronted with stubborn or overly hasty creditors, or creditors whose identities are unknown because of the existence of a large number of bonds in bearer form”); S. REP. No. 95-589, at 111 (1978) (same). A plan may not be confirmed unless it is filed in good faith. 11 U.S.C. § 901(a) (incorporating 11 U.S.C. § 1129(a)(3) into Chapter 9); id. § 1129(a)(3) requiring that plan be proposed “in good faith and not by any means forbidden by law”.)
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it was intended."  

The analysis in the Stockton and Detroit cases suggests that taxes are relevant to good faith, just as the decisions find taxes relevant to insolvency. Stockton did not directly mention the relevance of taxes when it held that Stockton proceeded in good faith, but the court did find that “the extent of the City’s prepetition efforts” to address its insolvency was a factor to be considered in determining good faith. The court focused on Stockton’s efforts to cut expenses in evaluating this factor.

Detroit expressly looked to taxes in deciding that the city’s prepetition efforts to address its debts were adequate. The court relied on the facts that the city had “increased the City’s corporate tax rate, worked to improve the City’s ability to collect taxes, and increased lighting rates” in finding that the city’s prepetition efforts supported a conclusion that the city acted in good faith.

At least one court has dismissed a Chapter 9 case because of a government’s failure to exercise its power to collect from its members. The court in In re Sullivan County Regional Refuse Disposal District dismissed a petition for lack of good faith because the debtors did not use their power to assess their members. The debtors in the case were two waste disposal districts, each with several towns and cities as members. The districts had formed a joint venture to contract with a


215. In San Bernardino, the court found that the municipality acted in good faith without analyzing possible tax increases, perhaps taking into account the fact that the city apparently did not realize the depth of its financial problems in time to seek a tax increase before filing for bankruptcy. See In re City of San Bernardino, 499 B.R. 776, 790 (Bankr. C.D. Cal. 2013) (“City cannot achieve a balanced budget unless it is allowed to reorganize its debt”); id. at 791 (“paucity of options for a City with such substantial, undisputed fiscal woes”). Apparently, San Bernardino was not aware of the depth of its problems until it had already run out of money to pay its employees. See id. at 780 (noting that the “first comprehensive report to the Common Council regarding the fiscal crisis” was July 10, 2012); id. at 790 (“City could no longer pay its employees on July 1st.”). It does not seem that San Bernardino had time to present a tax increase to the voters before running out of money.

216. See In re City of Stockton, 493 B.R. 772, 794 (Bankr. E.D. Cal. 2013). The Stockton court found that the city establishes a presumption of good faith by showing that it meets the other Chapter 9 eligibility requirements.

217. Id. at 795.


219. 165 B.R. 60 (Bankr. D.N.H. 1994); see also West Coast Life Ins. Co. v. Merced Irrigation Dist., 114 F.2d 654, 670 (9th Cir. 1940) (irrigation district’s failure to levy taxes was not bad faith where “[c]ontinued levying of taxes would result in ‘pyramiding’ debts upon the diminishing taxpayer acres”).

private company to build and operate an incinerator. The project was to be funded through operating revenues such as tipping fees, but the districts were obligated to the project operator and had the power to assess their member towns and cities for shortfalls. The districts did not even try to use this assessment power until the day before their bankruptcy filing, when the district boards both voted against an assessment to cover the shortfall.

The court found that the districts did not file their petition in good faith, although it agreed that “debtors . . . do not have to demonstrate that they have fully exercised their taxing powers to the maximum extent possible.” The court found that the districts failed the test because they “never exercised their assessment powers prior to coming into bankruptcy court” and “ignored any timely resort to their primary asset” (that is, their assessment power). The court’s summary of the districts’ misbehavior describes the type of opportunistic bankruptcy this Article addresses: “[t]he debtors created their own problem of a massive debt by signing a contract and then refusing to face up to their obligations under that contract with steadfast refusal to exercise their assessment powers.”

Other cases have found tax levels relevant but have rejected tax-level-based challenges to good faith because the municipality’s taxes were already high relative to its peers. Although one case may have rejected a good-faith challenge to a plan based on electoral infeasibility

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221. Id. at 65
222. Id. at 65–66.
223. Id. at 66.
224. Id. at 79 (districts did not negotiate in good faith); id. at 82 (districts did not file in good faith).
225. Id. at 78.
226. Id. at 78 (emphasis in original); id. at 82 (“steadfast refusal to exercise their assessment powers”).
227. Id. at 78.
228. Id. at 82.
229. In re Chilhowee R-IV Sch. Dist., 145 B.R. 981, 983 (Bankr. W.D. Mo. 1992) (holding that a school district facing large judgment for discharged teachers did not act in bad faith in filing Chapter 9 when “the school board [was] already assessing the highest levy in the county” and stating that “[t]o say that they had to institute the highest possible levy (requiring state approval) before taking any other action or be guilty of bad faith filing, is unreasonable”); In re McCurtain Mun. Auth., No. 07-80363, 2007 WL 4287604, at *6 (E.D. Okla. Dec. 4, 2007) (municipal water and sewer authority did not file in bad faith where water and sewer rates in the municipality were “significantly higher than rates in surrounding areas” and “it is unlikely that sufficient funds could have been generated through the imposition of higher water and sewer rates or an assessment on [local] citizens”). Such cases employ the “top of the range” standard discussed in more detail below. See infra Section IV.B.3.
alone, without substantively considering the level of taxes.\textsuperscript{230} the weight of authority supports the proposition that voters cannot simply walk away from obligations in bankruptcy without some judicial inquiry into taxation.

It is true that the good-faith requirement’s bite may be reduced by a rule, first articulated in \textit{Stockton} and followed in \textit{Detroit}, that the city establishes a presumption of good faith by showing that the other requirements for eligibility are met.\textsuperscript{231} The new rule effectively puts the burden of production of evidence of bad faith on the parties objecting to the plan.\textsuperscript{232} Nevertheless, it appears that taxation continues to be relevant to the substantive content of the good-faith standard.

\textbf{C. The “Best Interests of Creditors” Requirement: All That Creditors Can Reasonably Expect}

A bankruptcy court cannot confirm a municipal plan of adjustment unless the court finds that the plan “is in the best interests of creditors and is feasible.”\textsuperscript{233} Other scholars have suggested that this provision supplies the strongest basis for arguing that bankruptcy courts may condition relief on tax increases.\textsuperscript{234}

Although authority giving specific content to the phrase “best interests of creditors” is sparse, the text has been understood in a general sense to mean that creditors must receive all they “can reasonably expect to receive in the circumstances.”\textsuperscript{235} As one leading treatise reports, “[c]ourts have interpreted the test . . . to mean that the plan must be better for creditors than realistic alternatives . . . . A plan that makes little

\textsuperscript{230} See \textit{In re Corcoran Hosp. Dist.}, 233 B.R. 449, 459 (Bankr. E.D. Cal. 1999) (finding that it would be a “futile exercise” for the debtor hospital district to seek to increase assessments). The court did not state precisely why seeking a tax increase would be futile, but it did note the city manager’s testimony that voters would be unlikely to approve a tax increase to support the hospital district, despite the fact that “the residents . . . see [the hospital] as an essential element to the survival of Corcoran as a community.” \textit{Id.} at 454. The court’s interpretation can, however, be interpreted as resting on the legal incorrectness of an argument that “the debtor has the obligation under California law to maximize its taxing power in order to pay its creditors,” \textit{ibid.} at 459, rather than on electoral futility, \textit{see id.} at 459–60.


\textsuperscript{232} See \textit{Stockton}, 493 B.R. at 795 (explaining burden of production).


\textsuperscript{234} McConnell & Picker, supra note 3, at 474–75.

\textsuperscript{235} 6 \textit{COLLIER ON BANKRUPTCY}, supra note 52, ¶ 943.03[1][f][B], at 943-16. (stating that under the test, “it is not necessary that . . . taxes be increased”). The only authority cited for the latter proposition is \textit{Corcoran}, discussed \textit{infra}.
or no effort to repay creditors may not be in their best interests . . . ." 236

The court in Detroit found that tax levels are relevant to the “best interests of creditors” test, a point the city had conceded. 237 In its confirmation opinion, 238 the court “address[ed] the argument of some creditors that the City could pay them more by raising taxes." 239 The court found that Detroit was “simply unable to pay [its creditors] by raising taxes." 240 It credited testimony from the city’s chief financial officers that raising taxes “would not result in increased revenues” and that tax increases risked a “death spiral” wherein tax increases actually caused revenues to decrease. 241 In addition to this argument that tax increases were economically infeasible, the court also referenced its earlier ruling that tax increases were illegal. 242

As noted, the eligibility decision in Stockton anticipated a tax increase. 243 At confirmation, the court relied on the fact that the city had adopted sales tax increase “in the greatest amount and for the longest period permitted by California law” 244 and that the increase was integral


237. Consolidated Reply to Certain Objections to Confirmation of Fourth Amended Plan for the Adjustment of Debts of the City of Detroit at 74, In re City of Detroit, 504 B.R. 97, 180 (Bankr. E.D. Mich. 2013) (No. 13-53846) (noting that Detroit has “acknowledge[d] that it is appropriate for the Court to consider the City’s ability to levy additional taxes in considering whether the Plan should be confirmed”). Detroit argued that it should not be required to raise taxes because doing so would be futile, and therefore counterproductive, in light of the city’s already-high taxes and depressed condition. Detroit cited its “substantial and increasing rates of tax delinquency” in support of this argument, and noted that “the abundance of vacant, foreclosed, and abandoned properties in the City renders raising property taxes a fool’s errand.” Id. at 81–82. Notably, the parties arguing that the city should have sought higher tax revenues were bond insurers rather than representatives of pension beneficiaries.


239. Id. at 213.

240. Id. at 216.

241. Id. at 215; see also id. at 216 (citing testimony that “the City is at tax saturation and . . . raising taxes would likely add to the population decline”).

242. Id. at 216 (citing Detroit, 504 B.R. at 121, for the proposition that “the City cannot legally increase its tax rates”). The court buttressed its findings that tax increases were economically infeasible and legally impossible with a finding that they were electorally infeasible. Id. at 216 ("[T]he likelihood is remote that the people of Detroit or the state legislature would vote to raise taxes.").

243. In re City of Stockton, 493 B.R. 772, 790 (Bankr. E.D. Cal. 2013) ("[A] budget can be returned to solvency with a combination of debt adjustment and revenue enhancement, as appropriate to the particular situation.").

244. In re City of Stockton, 526 B.R. 35, 61 (Bankr. E.D. Cal. 2015).
to the city’s plan of adjustment.\textsuperscript{245} Although the court did not expressly tie the tax increase to the best interests test,\textsuperscript{246} its analysis suggests that the overall picture would have been different without the tax increase.

\textit{Stockton} and \textit{Detroit} are consistent with a rule that the “best interests of creditors” test includes consideration of tax levels, including what tax levels are economically and legally feasible. Such a rule is consistent with precedent, in particular with \textit{Kelley} and \textit{Fano}, the two cases that have a special place in the legislative history of the 1976 and 1978 Acts.\textsuperscript{247}

In \textit{Kelley v. Everglades Drainage District},\textsuperscript{248} the Supreme Court reversed an appellate decision affirming confirmation of a municipal bankruptcy plan on the ground that the district court had not made findings sufficient to allow appellate review of the decision to confirm.\textsuperscript{249} In particular, the court found that where debts are to be repaid from tax revenues, the court must consider “probable future revenues available for the satisfaction of creditors.”\textsuperscript{250} In the case at hand, “[a]ppropriate facts” to consider included past tax revenues, current rates, and the present assessed value of property, as well as “the probable effect on future revenues of a revision in the tax structure . . . , the extent of past tax delinquencies, and any general economic conditions of the District which may reasonably be expected to affect the percentage of future delinquencies.”\textsuperscript{251} The ability to raise revenues by raising taxes was relevant to confirmation of a plan.

The Ninth Circuit’s decision overturning confirmation of a composition\textsuperscript{252} in \textit{Fano v. Newport Heights Irrigation District}\textsuperscript{253} is even more pointed. Given that the irrigation district’s tax delinquency rate was less than five percent,\textsuperscript{254} the court stated:

\[W\]e are unable to find any reason why the tax rate should not

\begin{itemize}
  \item \textsuperscript{245} Id. at 62.
  \item \textsuperscript{246} See Stockton Transcript, \textit{supra} note 164, at 40–41 (interpreting best-interests standard to require “the best that is available under the circumstances”). The court did not expressly address the best-interests standard in its written opinion on confirmation. \textit{See Stockton}, 526 B.R. 35.
  \item \textsuperscript{247} \textit{See supra} Sections II.B.2 & II.B.3.
  \item \textsuperscript{248} 319 U.S. 415 (1943).
  \item \textsuperscript{249} Id. at 422.
  \item \textsuperscript{250} Id. at 420.
  \item \textsuperscript{251} Id. at 420–21 (emphasis added).
  \item \textsuperscript{252} A “composition” under the 1937 Act was the rough equivalent of a “plan of adjustment” under the current statute.
  \item \textsuperscript{253} 114 F.2d 563 (9th Cir. 1940).
  \item \textsuperscript{254} Id. at 565 n.2.
\end{itemize}
have been increased sufficiently to meet the District’s obligations or why it can be said that the plan is “equitable” and “fair” and for the “best interest of the creditors” with no sufficient showing that the taxing power was inadequate to raise the taxes to pay them.\textsuperscript{255}

\textit{Fano} certainly supports the proposition that taxes are relevant to plan confirmation; it could be read to go farther and require that taxes be raised as high as economically feasible before a plan is confirmed.

To be sure, at least one case has directly rejected a challenge to plan confirmation based on tax levels. In \textit{In re Sanitary & Improvement District No. 7},\textsuperscript{256} the bankruptcy court rebuffed bondholders’ contention that under the best interests test, it was the “duty of the [debtor] to levy sufficient taxes to pay the claims as they existed on the date of the petition plus accruing interest.”\textsuperscript{257} However, even this decision could be read as turning on the fact that tax increases would not raise revenue because the municipality had passed the peak of the “revenue hill.” The court found that trying to impose taxes that would pay the bondholders in full with interest “would create such a high level of taxes for the district and the homeowners that it is likely the revenues would not be made available to the district by taxpayers and the bondholders would still not be paid.”\textsuperscript{258}

Confirmed bankruptcy plans for municipal general governments, rare though they are,\textsuperscript{259} also support the proposition that taxes are relevant.\textsuperscript{260}

\begin{footnotes}
\textsuperscript{255} Id. at 565–66.
\textsuperscript{257} Id. at 974.
\textsuperscript{258} Id. at 976.
\textsuperscript{260} Considering tax levels as part of the best interests test is also the historical practice, at least according to Orange County’s lead bankruptcy counsel. See Adam J. Levitin, Experts Examine Municipal Financial Distress, AM. BANKER, INST. J., Dec. 2009–Jan. 2010, at 28, 79 (comments of Bruce Bennett) (“Historically, courts have gotten involved in deciding how much taxes have to be raised prior to the court confirming a plan that pays debt less than in full. They don’t do it directly, as the court doesn’t have the power to raise taxes, but the court has the power to approve a plan as being in the best interest of creditors. When considering whether a plan is in the best interest of creditors, the court decides whether a municipality has exerted extensive enough efforts to raise
Stockton, discussed above, is not the only city to have included a tax increase in its confirmed plan of reorganization. Indeed, where such increases are feasible, unlike in Detroit, they appear to the norm for confirmed plans. Jefferson County, Alabama’s bankruptcy, the largest municipal bankruptcy other than Detroit’s, was resolved with a plan that increased municipal sewer rates. One of the only two cities other than Detroit to have cut pensions in bankruptcy (Central Falls, Rhode Island) included tax increases in its confirmed plan. And most recently, the city in the largest pending bankruptcy, San Bernardino, California, has proposed a recovery plan calling for tax increases along with its plan of adjustment.

A more determinate version of the best-interests standard, embraced by some scholars and courts, is worth comment. In general, the


262. The city of Prichard, Alabama, population approximately 28,000, was the other. Its case was ultimately resolved by a plan of adjustment that ratified the settlement of a state-court lawsuit between retirees and the city. See Order Confirming Debtor’s Sixth Amended Plan of Adjustment of Debts Pursuant to Chapter 9 of the Bankruptcy Code, In re City of Prichard, No. 09-15000 (Bankr. S.D. Ala. July 8, 2014) [hereinafter 2014 Prichard Confirmation Order]; Sixth Amended Disclosure Statement of City of Prichard at 14–17, City of Prichard, No. 09-15000 (Jan. 24, 2014) (describing treatment of pension claims).

263. PEW CHARITABLE TRUSTS, THE STATE ROLE IN LOCAL GOVERNMENT FINANCIAL DISTRESS 41 (2013) (“Property taxes will go up 4 percent a year for the next five years in a city where the median income is about $34,000 a year.”); Fourth Amended Plan for the Adjustment of Debts of the City of Central Falls, Rhode Island at 34–36, In re City of Central Falls, No. 11-13105 (Bankr. D.R.I. July 27, 2012) (providing for periodic reporting of city budgets and attestation that budgets are in material conformity with “Six-Year Financial Projection” and providing that “any creditor . . . or [stakeholder] . . . is hereby granted standing to seek specific enforcement . . . from the Bankruptcy Court to ensure compliance with the Plan terms if the City or any other person or entity takes, or seeks to take, any action(s) which makes or would make the Plan not in Material Conformity with the Plan terms”); City of Central Falls, Six-Year Financial Projection FY2012-FY2017, at 8 (June 15, 2012) (“Property tax revenues are forecasted to grow at the maximum allowed according to R.I. Gen. Laws § 44-5-2, which is four and a quarter percent (4.25%) in FY2012 and four percent (4.0%) thereafter.”). The Central Falls plan of adjustment was not opposed.


265. See McConnell & Picker, supra note 3, at 466, 475–76; Frederick Tung, After Orange County: Reforming California Municipal Bankruptcy Law, 53 HASTINGS L.J. 885, 899 n.69 (2002).

266. See In re City of Detroit, 524 B.R. 147, 213 (Bankr. E.D. Mich. 2014) (applying the best-interests test and stating that “[t]he issue . . . is primarily whether the available state law remedies
remedy under nonbankruptcy law is said to be a writ of mandamus commanding the city to levy taxes that it is under a statutory or contractual duty to levy.\textsuperscript{267} It could be argued by analogy that a city satisfies the best-interests standard if the plan of reorganization gives creditors whatever they would have been able to receive in mandamus actions under state law. This suggestion can be seen as drawing on a kind of analogy to Chapter 11. Chapter 11 requires that a plan be as good for creditors as liquidation would be, and in that sense ensures that creditors get at least as much in a plan as they would get if they were to exercise their remedies under nonbankruptcy law.\textsuperscript{268}

There is a certain symmetry in adapting the Chapter 11 standard to the municipal context, but it is not clear that doing so honors the congressional intention that debts be paid if it is reasonably possible to do so. If a state enacts a remedial scheme that makes it difficult to collect against municipalities under nonbankruptcy law,\textsuperscript{269} it is by no means clear that the city should be able to take advantage of the weakness of that scheme to wipe away its debts in bankruptcy if the city would not default absent bankruptcy. Even under a weak state-law remedial scheme, a city’s preferences might be, in order from most to least preferred: (1) eliminate debts in bankruptcy, (2) pay debts in full, (3) default and be sued. For example, if a city cares about its reputation, it might not default, but might seek bankruptcy protection if doing so loses its stigma.\textsuperscript{270} A city should not necessarily be able to shed its debts in bankruptcy just because creditors would not recover effectively if they did sue, when in fact the city would pay debts rather than being sued if bankruptcy relief were not available.

\footnotesize{\textsuperscript{267} See McConnell & Picker, supra note 3, at 445–47 (discussing issuance of writs of mandamus requiring taxes where there was a “plain duty under state law or contract”).

\textsuperscript{268} See 11 U.S.C. § 1129(a)(7)(A)(ii) (2012) (providing that plan must promise nonconsenting creditors “not less than the amount such [creditor] would . . . receive or retain if the debtor were liquidated under chapter 7 of this title.”).

\textsuperscript{269} For example, California law apparently limits property taxes levied to pay voluntary debts to the 1% level provided by Proposition 13, CAL. GOV’T CODE § 971(b) (West, Westlaw through 2016 Reg. Sess.), a limit that would seem to impose a strict limit on the effectiveness of the mandamus remedy. See Ventura Grp. Ventures v. Ventura Port Dist., 16 P.3d 717, 722–24 (Cal. 2001) (holding that the County of Ventura could not, and could not be judicially ordered to, raise property taxes beyond the one-percent level in order to satisfy judgments arising out of the Ventura Port District’s breach of contract with a developer).

\textsuperscript{270} See supra note 83 and accompanying text.}
D. The “Fair and Equitable” Requirement: All That the Municipality Is Reasonably Able to Pay

If a Chapter 9 plan of adjustment is to be “crammed down,” that is, forced upon a nonconsenting class of impaired creditors, the court must find that the plan is “fair and equitable.” Commentators have noted that the “fair and equitable” standard may require more of taxpayers than the insolvency standard for bankruptcy eligibility, and Fano seems to suggest that taxes are relevant under the “fair and equitable” test as well as the “best interests” test.

Another case from the same era as Fano, also endorsed in the legislative history of the 1976 Act, expressly evaluates taxes in connection with the fair and equitable requirement for confirmation. In Lorber v. Vista Irrigation District, the court found that the “fair and equitable” requirement meant that bondholders were entitled to “all that they [could] reasonably expect in the circumstances,” and that to satisfy this standard, there should be an evidentiary finding that the plan of adjustment calls for payment of “all that the District is reasonably able to pay in the circumstances.” The ability to levy taxes is part of reasonable ability to pay, as the Supreme Court held in Kelley. In that case, the Court stated that a determination of the overall fairness of a plan requires consideration of “probable future revenues available for the satisfaction of creditors.”

271. See 11 U.S.C. § 901(a) (incorporating section 1129(b)(1) into Chapter 9 by reference); id. § 1129(b)(1) (providing that plan can be confirmed without consent of all impaired classes (“crammed down”) if certain requirements are met, including a requirement that the plan be “fair and equitable”). Prior to the 1978 Act, all municipal bankruptcy plans, not just those that were going to be crammed down, had to meet the “fair and equitable” standard. See Act of Apr. 8, 1976, Pub. L. No. 94-260, § 94(b)(1), 90 Stat. 315, 323 (requiring a plan be “fair and equitable” to be confirmed).

272. See, e.g., 6 COLLIER ON BANKRUPTCY, supra note 52, ¶ 900.02[c], at 900-22 n.70 (noting that, unlike the eligibility requirement of insolvency, “the fair and equitable rule, if invoked, requires use of the taxation power to the fullest extent.”); Lawrence P. King, Municipal Insolvency: The New Chapter IX of the Bankruptcy Act, 1976 DUKE L.J. 1157, 1174 (1976) (suggesting that, in municipal cases, “[t]he fair and equitable and feasible test should more properly involve a comparison between the expenditures and the income necessary for the particular municipality, considering in the assessment of income the extent to which taxes can be raised and obtained”).

273. Fano v. Newport Heights Irrigation Dist., 144 F.2d 563, 565–66 (9th Cir. 1940) (mentioning both standards).


275. 127 F.2d 628 (9th Cir. 1942).

276. Id. at 639 (citing cases supporting this proposition).

277. Id.

As discussed in this Part, several provisions of the Bankruptcy Code arguably require courts to take tax levels into account in determining whether to confirm a plan or whether the municipality is eligible for bankruptcy relief in the first place. By and large, the courts have taken tax levels into account when interpreting these provisions. In so doing, the courts have acted in a way consistent with the intent of Congress as expressed in the legislative history discussed in the previous Part.

IV. SHARPENING THE RELATIONSHIP BETWEEN TAX LEVELS AND DEBT RELIEF IN FEDERAL BANKRUPTCY COURT

The legislative history thus suggests that Congress intended for municipal tax levels to be relevant in deciding whether a municipality is eligible for bankruptcy and in deciding whether to approve the municipality’s plan of adjustment. The case law illustrates that courts have on the whole followed Congress’s intention by taking taxes into account for both bankruptcy eligibility and plan confirmation. Yet neither the case law nor the legislative history provides a precise answer to the question of just how courts are to analyze municipal taxes in bankruptcy.

Before turning to that question, this Part briefly addresses the argument that courts are not permitted to take tax levels into account because doing so impermissibly invades municipal autonomy. Although this argument apparently has not gained traction in the courts and although the legislative history contains at least some suggestion that it is incorrect, it arguably received a boost from the Supreme Court’s recent decision applying the unconstitutional conditions doctrine in National Federation of Independent Business v. Sebelius. If it is

679 (9th Cir. 1940) (affirming plan confirmation where expert report “entailed a scientific study of the tax paying ability of the District” and “support[ed] the conclusion that 51.501 cents on the dollar [the amount provided in the plan] is fair and equitable and all that could reasonably be expected in all the existing circumstances”); Moody v. James Irrigation Dist., 114 F.2d 685, 689 (9th Cir. 1940) (affirming confirmation of plan where testimony of a longtime local resident and member of the California Districts Securities Committee testified that the amount provided in the plan was “well up to the limit of the ability of the lands in the District to meet”); Bekins v. Lindsay-Strathmore Irrigation Dist., 114 F.2d 680, 685 (9th Cir. 1940) (based on district’s tax delinquency rate and “tabulations of tax performance” in the record, the amount provided in the plan was “all that the bondholders can reasonably expect in the circumstances”); Jordan v. Palo Verde Irrigation Dist., 114 F.2d 691, 695 (9th Cir. 1940) (noting that based on valuation testimony of two agricultural economists, value of land was such that the plan was fair and equitable in light of the “probable ability of the land to pay in the future”).

impermissible for Congress to condition Medicaid spending on Medicaid expansion, perhaps it is also impermissible for Congress to condition municipal bankruptcy relief on the municipality’s achieving certain tax levels. Although a full analysis of the constitutional issue is beyond the scope of this Article, the Part argues briefly that municipal bankruptcy is different from the context at issue in Sebelius in several respects that scholars have found important in applying unconstitutional conditions.

Having rejected the argument that taxes may not be taken into account, this Part then evaluates three particular ways courts could go about taking taxes into account, all three of which find some support in the cases. Two of these approaches refer to absolute tax levels. The first would prescribe that taxes be raised to the revenue-maximizing level (the “top-of-the-hill” criterion). The second would require that taxes be at the top of a range of comparable municipalities (the “top-of-the-range” criterion). A third approach focuses not on the absolute level of taxes, but on whether the plan of adjustment calls for significant additional taxes beyond what the city is already charging. The Article calls this the “share-some-pain” criterion. This Part argues that a combination of the three tests deserves consideration: a municipality’s failure to tax at the top of the range before bankruptcy should weigh against eligibility unless tax increases would not increase revenues (that is, the municipality is past the top of the hill) or bankruptcy would enable a solution that gets taxes to the top of the range (that is, bankruptcy entails sharing pain to a specified extent).

A. Potential Limits on the Bankruptcy Court’s Power to Influence Municipal Taxes: Sections 903 and 904 and the Tenth Amendment

Scholars have argued that sections 903 and 904 of the Bankruptcy Code limit the court’s power to take taxes into account in municipal bankruptcy.280 Section 903 preserves “the power of a State to control...a municipality of...such State in the exercise of [its] political or governmental powers.”281 Section 904 forbids the court from “interfer[ing] with” the municipality’s “political or governmental

280. See, e.g., McConnell & Picker, supra note 3, at 472 (stating that section 904 “[p]resumably...precludes the bankruptcy court from exercising the principal common law judicial remedy for nonpayment of debts—the order to raise taxes”); Kordana, supra note 90, at 1059 (“A judicially-compelled tax increase would thus appear to run afoul of Section 904, as might the frustration of a municipality’s ability to use Chapter 9 if it did not comply with the judge’s desire for a tax increase.”).
powers” or “revenues,” “unless the debtor consents or the plan so provides.”

Thus, section 903 preserves state authority over municipalities and section 904 preserves local autonomy as against the court.

It is possible that, by refusing to confirm a plan that does not include tax increases or finding that a debtor is ineligible for bankruptcy because it refuses to consider tax increases, a court impairs state authority over municipalities in violation of section 903 or “interfere[s] with” the debtor’s “political or governmental powers” or “revenues” in violation of section 904. Collectively, these contentions can be called the “interference argument.”

It does not appear that any court has embraced the interference argument, and the legislative history of the municipal bankruptcy statutes does not seem to support it. Although the history contains a number of general affirmations of state power over municipalities that apparently add little to the statutory text itself, there is very little discussion of the interaction between the no-interference principle articulated in general terms in sections 903 and 904 and the taxes-relevant principle affirmed elsewhere in the legislative history and

282. Id. § 904.

283. The restrictions contained in sections 903 and 904 have been part of the municipal bankruptcy statutes from the beginning. For section 903, see Act of May 24, 1934, Pub. L. No. 73-251, § 80(k), 48 Stat. 798, 802–03 (preserving state authority in language of § 903); Act of Aug. 16, 1937, Pub. L. No. 75-302, § 83(i), 50 Stat. 653, 659 (same); Act of Apr. 8, 1976, Pub. L. No. 94-260, § 83, 90 Stat. 315, 316–17 (same). For section 904, see Act of May 24, 1934, § 80(c)(11), 48 Stat. at 801 (limiting court’s power in language of § 904); Act of Aug. 16, 1937, § 83(c), 50 Stat. at 657 (same); Act of Apr. 8, 1976, § 82(c), 90 Stat. at 316 (same). There seems to have been no intent to change the meaning of these provisions with adoption of the 1978 Act. Compare Act of Nov. 6, 1978, Pub. L. No. 95-598, § 903, 92 Stat. 2549, with Act of Apr. 8, 1976, § 83; compare Act of Nov. 6, 1978, § 904, with Act of Apr. 8, 1976, § 82(c); H.R. Rep. No. 95-595, at 397 (1977) (stating that new section 903 “is derived, with stylistic changes, from section 83”); id. at 398 (stating that section 904 “adopts the policy of section 82(c) of current law” and “[t]he only change in this section from section 82(c) is to conform the section to the style and cross-references of H.R. 8200.”). See also 124 CONG. REC. 32403 (1978) (statement of Rep. Edwards) (explaining that, as a result of discussions between House and Senate leaders, “[t]o the extent Section 903 of the House bill would have changed present law, such section is rejected”); id. at 17416 (statement of Sen. DeConcini) (concluding the same).

284. See H.R. Rep. No. 95-595, at 264 (“[R]ecent decision of the Supreme Court in Usery stressing the concept of non-interference by the Federal government with State governmental powers.”); id. at 398 (“[T]he court may not interfere with the choices the municipality makes as to what services and benefits it will provide to its inhabitants.”); 134 CONG. REC. 24461, 24584 (1988) (statement of Sen. DeConcini) (stating that, in recognizing special treatment of revenue bonds in bankruptcy, 1988 Act protects “the underlying scheme of State constitutional laws” under which “each State has developed its own set of powers, restrictions, and limitations on the financing of State and local services”).
effectuated through the four statutory provisions discussed earlier.  

One salient piece of the history of the 1976 Act does suggest that a court does not interfere with state and municipal power if it imposes conditions on relief, because the municipality consents to such conditions by seeking bankruptcy relief in the first place. In explaining proposed section 805(e) of S. 2597, the Ford Administration’s proposal for municipal bankruptcy for large cities, which contained virtually identical language to section 904, then-Assistant Attorney General Scalia stated:

The court’s influence over what the city may do exists only because the court may obtain the city’s voluntary agreement to certain actions in order to obtain debt certificates or in order to get the plan approved as being a feasible plan and one that will result in a fiscally sound city budget.

But the judge has no authority by reason of the proceeding to say you do this, you do not do that, and this is how the city runs. He obtains that authority only because the city voluntarily agrees to certain of these actions in order to obtain measures that it wants from the court or to get a certain type of plan finally approved by the court.  

Thus, at least one (deceased) Justice of the Supreme Court has argued that judges can attach conditions to relief that cities seek without violating the Bankruptcy Code provision preserving municipal autonomy. Scalia made the argument while acting as an administration official, but when given the legislative history, the precedents for taking tax levels into account, and the absence of precedent supporting the interference argument, it seems doubtful that the interference argument succeeds as a matter of statutory interpretation.

But even if requiring tax increases as a condition of bankruptcy relief complies with the Bankruptcy Code, there may still be a constitutional

285. See supra Part 0
287. 1975 Subcommittee Hearings, supra note 95, at 217 (statement of Assistant Att’y Gen. Scalia). The references to fiscally sound budgets refer to provisions of the administration’s proposal that were not adopted in the enacted legislation. See Act of Apr. 8, 1976, Pub. L. No. 94-260, 90 Stat. 315, see also 11 U.S.C. § 904 (providing that bankruptcy court may not interfere with political or governmental powers of debtor “unless the debtor consents or the plan so provides”); S. REP. NO. 95-989, at 110 (1978) (noting that the section reserving state power to control municipalities “provides that the municipality can consent to the court’s orders in regard to use of its income or property. It is contemplated that such consent will be required by the court for the issuance of certificates of indebtedness . . . . Such consent could extend to enforcement of the conditions attached to the certificates or the municipal services to be provided during the proceedings”).
question. Conditions the federal government attaches to benefits it confers may be unconstitutional even when states “voluntarily” accede. Although a complete discussion of the constitutional issues presented is beyond the scope of this Article, a preliminary look suggests that bankruptcy courts could require tax increases as a condition of bankruptcy relief without violating the unconstitutional-conditions doctrine. This is so even after that doctrine’s recent reinvigoration in National Federation of Independent Business v. Sebelius, which held it unconstitutional for Congress to condition states’ Medicaid funding on their expansion of the program.

Most unconstitutional-conditions decisions about the limits of federal power to induce state action arise in markedly different contexts from municipal bankruptcy; most notably, they have arisen under the Spending Clause. Even granting that an analogy can be drawn between conditioning federal spending on state acquiescence to federal policies and conditioning federal bankruptcy relief on municipal acquiescence to federal policies, it seems doubtful that conditioning bankruptcy relief on certain tax levels would be unconstitutional.

Professor Samuel Bagenstos has interpreted Sebelius in light of previous scholarship on the unconstitutional-conditions doctrine, concluding that three criteria must be met before a conditional spending

288. See Nat’l Fed’n of Indep. Bus. v. Sebelius, __ U.S. __, 132 S. Ct. 2566, 2657, 2662 (2012) (noting that the Affordable Care Act “does not legally compel the States to participate in the expanded Medicaid program” but finding that the Act nonetheless “crosses the line from enticement to coercion”).

289. In addition to the unconstitutional-conditions argument addressed in the text, it might be argued that considering tax levels in determining whether to grant bankruptcy relief violates the separation of powers. Such an argument would have to contend with Missouri v. Jenkins, 495 U.S. 33 (1990), which held that the federal judiciary may order municipalities to raise taxes, id. at 55–56, even when state law purports to require a popular vote on the type of tax increase in question. Id. at 38; see also Bylinski v. City of Allen Park, 8 F. Supp. 2d 965 (E.D. Mich. 1998), aff’d, 169 F.3d 1001 (6th Cir. 1999) (rejecting challenge to consent decree requiring local tax increases, where challenge was on ground that state constitutional tax limits made the consent decree unlawful). It might be argued that Jenkins is inapplicable to tax levels in municipal bankruptcy because it dealt with federal courts’ remedial powers, but the Court relied on the remedial setting only in addressing a Tenth Amendment objection to imposition of taxes by a federal court, not a separation-of-powers objection. 495 U.S. at 55. As explained in the text, a Tenth Amendment challenge to federal courts’ ability to consider tax levels in bankruptcy appears weak for other reasons.


291. See, e.g., id. at 2662 (finding conditions on federal spending unconstitutional); Kathleen M. Sullivan, Unconstitutional Conditions, 102 HARV. L. REV. 1413, 1416–17 (1989) (listing unconstitutional-conditions challenges to federal spending).

program of Congress will be found unconstitutional: “[w]hen Congress takes an (1) entrenched federal program (2) that provides large sums to the states and (3) tells states that they can continue to participate in that program only if they also agree to participate in a separate and independent program, the condition is unconstitutionally coercive.”

Conditioning municipal bankruptcy relief on taxes does not clearly raise any of the issues Bagenstos identifies. First, considering taxes does not change the terms of an entrenched federal program, as taxes have been relevant to municipal bankruptcy relief from the beginning and states and municipalities cannot claim reliance on any particular version of the taxes-are-relevant requirement because there have not been enough cases to clearly ensconce any particular standard. Second, municipal bankruptcy is not analogous to a program that provides large sums to states because the total dollar amount of relief that has been afforded is quite small relative to state budgets and because the program is not too attractive to turn down; indeed, almost half of states in fact have turned it down. Third, tax levels are not separate

294. Id. at 874 (calling this the “no-new-conditions” principle); see also Seth F. Kreimer, Allocation Sanctions: The Problem of Negative Rights in a Positive State, 132 U. PA. L. REV. 1293, 1359 (1984) (“Losing a benefit previously provided seems different from simply never having been provided the benefit in the first place.”).
295. See supra Section II.A.
296. It could be argued that the tax-related requirement was not explicit enough. See, e.g., Pennhurst State Sch. & Hosp. v. Halderman, 451 U.S. 1, 17 (1981) (requiring conditions on federal spending to be imposed “unambiguously”). However, Pennhurst recognizes that legislative history can provide the required clarity. Id. at 18 (“[W]e find nothing in the Act or its legislative history to suggest that Congress intended” to impose the condition at issue in the case.).
298. The gist of the “provides large sums” portion of the test is that states do not have a real choice to turn down federal funding if the amounts on offer are large enough. See Bagenstos, supra note 293, at 874 (calling this the “too-big-to-refuse” principle); Sebelius, 132 S. Ct. at 2605 (states had “no real option” but to expand Medicaid eligibility with ten percent of state budgets at stake).
299. See H. SLAYTON DABNEY, JR. ET AL., MUNICIPALITIES IN PERIL 11 (2012) (“Approximately half of the states do not permit municipalities to file at all.”). Contrast the situation in South Dakota v. Dole, 483 U.S. 203, 211 (1987), in which the Court found that Congress had not deprived states of the “freedom of the will” to decide the drinking age, even though all fifty states raised the
and independent from bankruptcy; making funds available to pay creditors is not just germane, but central to bankruptcy.

B. Implementing the Idea That Taxes Are Relevant

This Section evaluates three possible specific ways, all suggested by the cases, of further specifying the notion that taxes are relevant: the “top-of-the-hill” criterion, which would require cities to raise taxes to the level that maximizes revenues, the “share-some-pain” criterion, which would require a substantial tax increase from existing levels, and the “top-of-the-range” criterion, which would require that taxes be at the top of a range of peer cities’ tax levels before cities can reduce their debts.

This Section argues that a combination of the three tests deserves consideration. If a city is not at the top of a relevant comparison range, that should weigh heavily in determining that the city is not eligible for bankruptcy unless the city can explain the situation. Permissible explanations could include demonstrating that tax increases would not increase revenue, that tax increases are legally forbidden, or that bankruptcy is itself necessary for voter approval of tax increases.

Courts that prefer to phrase the test more crisply could adopt a rebuttable presumption of bad faith in filing or bad faith insolvency that is triggered when the city does not tax to the top of the range. In this formulation, the presumption could be rebutted by proof that tax increases would not raise money, are prohibited, or can be achieved only through bankruptcy.

Likewise, at plan confirmation, a court should be prepared to find—perhaps via a rebuttable presumption—that a plan that does not put the city at the top of a relevant comparison range is not in the best interests of creditors and is not fair and equitable to dissenting impaired classes drinking age to twenty-one, just as Congress desired. Id.

300. Cf. Sebelius, 132 S. Ct. at 2605–06 (noting that Medicaid-expansion provisions were a “shift in kind, not merely in degree,” resulting in what was “in reality a new program”).

301. Professor Charles Tabb points out the importance of creditor recovery in both liquidation and rehabilitation bankruptcy cases. See CHARLES JORDAN TABB, THE LAW OF BANKRUPTCY 3 (3d ed. 2014) (“Liquidation bankruptcy cases serve two independent purposes: relief of debtors, and equitable treatment of creditors.”); id. at 6 (noting that, in rehabilitation cases, “all [creditors] may benefit from capturing a going-concern surplus out of the debtor’s future positive earnings”).

302. This exception assumes that state laws requiring electoral approval of taxes are not preempted in bankruptcy. At least one court has found that state-law electoral approval requirements survive in bankruptcy. See In re City of Stockton, 526 B.R. 35, 53–54 (Bankr. E.D. Cal. 2015).
unless the city can proffer an explanation.\textsuperscript{303} Given Congress’ concern that local populations and communities might abuse bankruptcy, it is much more doubtful that electoral impossibility, standing alone, should be an acceptable explanation. Even if bankruptcy courts cannot order tax increases and even if state electoral approval requirements are valid in bankruptcy in light of the Supremacy Clause, courts are not required to lend their imprimatur to a plan that discharges debts when local taxpayers are not doing their part.

The criteria set forth here apply to taxes and not spending. As a practical matter, most general-purpose cities that have entered bankruptcy have cut discretionary spending to the point where service levels are low,\textsuperscript{304} and there are probably limits on how far spending cuts can go, assuming cities must provide some minimal level of service.\textsuperscript{305} Thus, it makes sense to look to taxes as a source of creditor recovery. Moreover, much of the legislative history addresses taxes specifically, as opposed to spending.\textsuperscript{306} In light of these facts, it makes sense to discuss a tax-specific standard, although it is possible that bankruptcy law does require spending cuts in some circumstances.\textsuperscript{307}

In reviewing these proposed criteria, it is important to keep in mind that they do not represent general guides to tax policy. This Article does not argue that cities generally should tax to the top of their peer range or that tax increases are presumptively desirable in general. Instead, the Article has argued that, in the very specific context where a municipality seeks to invoke the federal bankruptcy power to eliminate valid debts, Congress intended that the city’s actual and potential revenues are relevant to the solution.

Thus, the tests discussed here do not specify what tax levels are

\textsuperscript{303}. If a city successfully argued at the eligibility stage that it should be allowed to file bankruptcy because that is the only way it can raise taxes, that presumably would be an independent ground to require the city to tax to the top of the range at confirmation. This could be accomplished through the requirement that plans be filed in good faith. See 11 U.S.C. § 901 (2012) (incorporating 11 U.S.C. § 1129(a)(3) into Chapter 9 by reference); id. § 1129(a)(3) (requiring that the plan be “proposed in good faith and not by any means forbidden by law”).

\textsuperscript{304}. See supra notes 28–32 and accompanying text.

\textsuperscript{305}. See Anderson, supra note 26, at 1188–95 (discussing city residents’ entitlements to services in bankruptcy).

\textsuperscript{306}. See supra Part 0

\textsuperscript{307}. The Detroit and Stockton courts both pointed to “service delivery insolvency,” the delivery of a critically low level of city services, as integral to their determinations that the insolvency test of 11 U.S.C. § 109(c)(3) was met. See \textit{In re City of Detroit}, 504 B.R. 97, 170 (Bankr. E.D. Mich. 2013); \textit{In re City of Stockton}, 493 B.R. 772, 789–90 (Bankr. E.D. Cal. 2013). Although these cases do not state in clear terms that bankruptcy eligibility requires service delivery insolvency, they do suggest that service levels are relevant to the insolvency determination, at least in some cases.
desirable or “affordable” in the general sense of the term. Instead, the tests specify what tax level is so unaffordable that charging it is a worse alternative than having a bankruptcy court lend its imprimatur to the city’s failure to meet legitimate obligations to bona fide creditors. Municipal insolvency creates suffering, and the criteria discussed here are guides for sharing that suffering in light of Congress’s objectively manifested intent. They are not policy prescriptions for cities that are financially healthy, or even for distressed municipalities that are not seeking federal bankruptcy protection.

1. “Top of the Hill”

One criterion that has at least indirect support in the legislative history and case law is the “top-of-the-hill” criterion, which would require that a municipality raise taxes to the revenue-maximizing level, either before filing as a condition of eligibility or after filing as a condition of plan confirmation. The criterion thus incorporates the assumption that increasing tax rates beyond a certain point—beyond the “top of the hill,” or the “peak of the Laffer Curve”—actually reduces the amount of revenue the taxes generate. The criterion is easy to articulate and to understand on a conceptual level and holds out the promise of objective application.

Implementation of the top-of-the-hill criterion is likely to be a challenge for courts. There are questions arising from the different types of taxes and their interaction. (For instance, if a city sets its sales tax at the revenue-maximizing level, should it also have to adopt a hotel excise tax? What if increasing the revenue from one tax decreases the revenue from others?) But the bigger challenge lies in coming up with a credible estimate of the revenue hill itself. How is a court to know if a 10% property tax will encourage residents to move out and depress property values enough so that it yields less revenue than a 9.5% property tax?

This challenge, though daunting, does not appear to be categorically more difficult than other factual questions law endeavors to answer, often with the help of expert testimony. For example, antitrust law requires courts to determine whether the effect of combining two firms

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308. General references to the “maximum capacity to pay,” see supra Section II.A, or to paying “to the fullest extent possible,” see supra Section II.B, can be interpreted as reflecting the top-of-the-hill criterion. There are also occasional more explicit references in the legislative history to the concept. See, e.g., supra note 131 and accompanying text.


310. For an explanation of the Laffer Curve, see supra note 113.
“may be substantially to lessen competition, or to tend to create a monopoly.”311 This often requires complex and deeply contestable analyses of competition and market power. For example, a federal district court evaluating the proposed merger of Staples and Office Depot undertook to determine whether a small but significant price increase in Staples’ prices would “cause a significant number of consumers to turn to non-superstore alternatives for purchasing their consumable office supplies”312—a hypothetical inquiry that required consideration of thousands of items of inventory across the locations of two nationwide chains.313 Within bankruptcy law, courts in corporate reorganization cases routinely face intimidating valuation challenges,314 such as appraising Lehman Brothers’ derivative positions.315 Indeed, determining the subjective intent of a human actor—a question the judicial system answers thousands of times each day—is arguably less tractable than doing the kind of tax analysis the top-of-the-hill test calls for.316 Given that empirical work on how to determine the top of the hill already exists,317 parties presumably would be able to proffer expert

312. Id. at 1076 (discussing price samples considered by court, including one accounting for ninety percent of Staples’ sales and another of approximately 2000 items). More recently, the Bazaarvoice court was called upon to decide, among other things, whether firms such as Google, Facebook, and IBM would constrain the market power Bazaarvoice would achieve in the business-to-business review and rating market as a result of its acquisition of rival PowerReviews. See United States v. Bazaarvoice, Inc., No. 13-cv-00133-WHO, 2014 WL 203966, at *38–54 (N.D. Cal. Jan. 8, 2014). This analysis does not seem qualitatively more difficult than the analysis of tax effects the top-of-the-hill test requires.
313. See, e.g., RICHARD A. POSNER, ECONOMIC ANALYSIS OF LAW 546 (8th ed. 2011) (noting that, if creditors object to proposed plan, “it is up to the “bankruptcy court to determine what the true value of the corporation is”); Anthony J. Casey, The Creditors’ Bargain and Option-Preservation Priority in Chapter 11, 78 U. CHI. L. REV. 759, 801 n.167 (2011) (discussing competing expert testimony relating to valuation of Calpine Corporation in its bankruptcy, with range of values from $11.9 to $25.5 billion).
testimony on the relevant questions.

Thus, although the top-of-the-hill criterion is probably harder to apply than other tests, that issue is not totally disqualifying. The more fundamental problem with the top-of-the-hill criterion is that the notion that financially strapped cities really are obligated to use every last ounce of their taxing power to get revenues is so extreme. Despite the indirect support for the test in some legislative and judicial statements, no court has actually gone so far as to embrace it unequivocally, and congressional statements that could be read as endorsing the standard could be discounted as rhetorical excess.

2. “Share Some Pain”

The Stockton confirmation opinion repeatedly mentions the fact that Stockton increased its sales tax as part of its plan of adjustment.\(^{318}\)

Indeed, the opinion emphasizes that the sales tax increase was the largest and longest-lasting sales tax increase possible under California law.\(^{319}\)

The exact role of the tax increase in the Stockton court’s reasoning is open to debate: the court cited the tax increase as a reason that there would be enough money to fund Stockton’s plan,\(^{320}\) but also arguably found that the tax increase supported the overall fairness of the settlement.\(^{321}\) Nevertheless, Stockton suggests the possibility of a standard based not on absolute tax or revenue levels, but on whether there is a substantial increase in taxes during the bankruptcy.

Requiring a nontrivial tax increase from current levels has some merit as a way of implementing Congress’s desire that courts incorporate revenues into their analysis of municipal bankruptcy. By imposing some level of sacrifice on the populace, the requirement goes some way toward meeting Congress’s requirement that populations pay all they reasonably can before taking advantage of bankruptcy protection. But there are two problems with the criterion. First, unless the court adopts

\(^{283}\) n.10).

\(^{318}\) In re City of Stockton, 526 B.R. 35, 54, 61–62 (Bankr. E.D. Cal. 2015); Stockton Transcript, supra note 164, at 19, 34.

\(^{319}\) Stockton, 526 B.R. at 61.

\(^{320}\) Id. (“The ability to pay the capital market creditors the agreed amounts contemplated a tax increase that, under California law, required a vote of the people.”); Stockton Transcript supra note 164, at 34 (“I am satisfied that there are adequate means for the Plan’s implementation, and particularly that the taxpayers have stepped up and approved the measure that added a local sales tax to the extent permitted by California law . . .”)

\(^{321}\) Stockton, 526 B.R. at 53–54 (describing tax increases in context of mediated compromise); Stockton Transcript, supra note 164, at 19 (contrasting settlement involving tax increase with assertion that pensions should be impaired).
the unlikely interpretation that a city must implement the highest legally permitted tax increases, the test is not determinate. It is not clear just how large a tax increase would be required to satisfy the standard. Second, it seems that the standard imposed by Congress is based on absolute tax levels, rather than the amount taxes are increased in the bankruptcy itself. The legislative history and case law nowhere suggest that absolute tax levels are irrelevant, as would be implied by strict application of the share-some-pain criterion and only the share-some-pain criterion.

3. “Top of the Range”

Cases that evaluate a municipality’s tax level relative to taxes in peer communities suggest a third standard, the “top-of-the-range” standard. For example, the court in In re Town of Westlake referred to tax rates in other cities, including Fort Worth and a set of “comparable cities,” not to the legal or economic maximum. Similarly, the court in In re Chilhowee R-IV School District supported its finding that the municipality acted in good faith by noting that “the school board [was] already assessing the highest levy in the county.” Another court, in In re McCurtain Municipal Authority, found that a municipal water and sewer authority did not file in bad faith where the authority’s water and sewer rates were “significantly higher than rates in surrounding areas.”

The “top-of-the-range” criterion would require that a municipality tax at a higher level than its peers before the municipality would be able to

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322. See supra Part 0
323. In re Town of Westlake, Texas, 211 B.R. 860, 867 (Bankr. N.D. Tex. 1997). The court concluded that the “maximum realized tax revenues” from an ad valorem tax would be $40,000 to $80,000, apparently corresponding to a rate of $0.50 to $1.00. This figure is below the “maximum permissible tax rate” of $1.50 per $100 valuation. The court apparently drew the endpoints of its $0.50 to $1.00 rate range from comparisons to other cities. The high end of the court’s range, $1.00, apparently came from a comparison to Fort Worth, which had a rate of $0.98, which the court described as being “on the high side.” The low end of the court’s range, $0.50, is the approximate midpoint of a range of “comparable cities.” The comparable-city range ran from $0.35 to $0.60.
324. In re Chilhowee R-IV Sch. Dist., 145 B.R. 981, 983 (Bankr. W.D. Mo. 1992). (noting that the school district facing large judgment for discharged teachers did not act in bad faith: “[t]o say that they had to institute the highest possible levy (requiring state approval) before taking any other action or be guilty of bad faith filing, is unrealistic”).
325. In re McCurtain Mun. Auth., No. 07-80363, 2007 WL 4287604, at *6 (Bankr. E.D. Okla. Dec. 4, 2007) (holding that the municipal water and sewer authority did not file in bad faith where water and sewer rates in the municipality were “significantly higher than rates in surrounding areas” and “it is unlikely that sufficient funds could have been generated through the imposition of higher water and sewer rates or an assessment on [local] citizens”).
adjust its debts in bankruptcy. If the municipality did not meet the
criterion before bankruptcy, the municipality would have to do so as a
condition of plan confirmation. Specifically, applying the criterion
would require constructing a peer group, establishing a basis for
comparing tax levels among the peers, and determining whether the
debtor’s tax levels were high enough in light of the comparison.

Applying the top-of-the-range criterion would not be totally
straightforward and uncontestable. Disputes could occur at each of the
three stages of application: assembling the peer group, constructing the
comparable measure of tax levels, and evaluating whether the debtor’s
tax levels are high enough relative to its peers’.

Construction of the comparison group necessarily would be case-
specific. The point is to assemble a group of cities with similar ability to
raise tax revenue, or fiscal capacity. It is impossible to assess the debtor
against a group of totally identical cities, but there should be some effort
to control for the major determinants of ability to raise tax revenue. For
example, states vary greatly in their tax regimes, so that in a typical
case it would seem to make sense to compare the debtor against
municipalities in its own state. Likewise, special districts should be
compared with special districts of the same type, and for general
governments to be compared with general governments.

The debtor should be compared to cities of comparable income levels
and property values, as these characteristics both are the bases for
taxation and likely measure the ability to pay taxes. Economists have
already devised a measure that may be useful in this regard: the
Representative Tax System approach, which “measures local tax
capacity by applying average—or ‘representative’—tax rates to all tax
bases that local governments are authorized to tax.”

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326. See, e.g., Bo Zhao, The Fiscal Impact of Potential Local-Option Taxes in Massachusetts 2–3
allow local-option taxes, and that thirty-six states impose local general sales taxes, twenty-seven
states allow local jurisdictions to impose meals taxes, and that fourteen states collect revenues from
local income or payroll taxes).

327. To the extent that a major metropolis such as Detroit is sui generis, this requirement might
have to be relaxed and the city might have to be compared to national peers, with adjustments made
for differing state tax regimes. It is not clear that major cities really are sui generis under an
approach like the Representative Tax System, however.

328. Zhao, supra note 326, at 7 (citing several other articles that make use of the Representative
Tax System).
compared with all other cities that may tax property and income only. Use of this method depends on assuming that tax capacity as measured by the Representative Tax System is a good proxy for ability to pay.

Another area on which parties and courts could draw in applying the top-of-the-range criterion is “interest arbitration,” a process that is widely used for determining public-sector wages when collective bargaining does not reach an agreement, particularly when employees are not allowed to strike.329 Interest-arbitration statutes typically direct the arbitrator to consider the public employer’s ability to pay,330 and the evidence that is considered on that score typically entails comparisons with other cities,331 often on the basis of similarities of population, scope of duties, and location.332

As the foregoing suggests, it will be crucial in creating the comparison group to decide whether the comparison group should be composed of cities with comparable service levels. If service levels are not taken into account, then the debtor might be required to impose higher taxes as a condition of relief just because citizens in an otherwise comparable city wanted higher service levels and therefore adopted higher taxes. The argument that it is unfair to require higher taxes on the debtor just because its peer happened to want more services might be countered in part by observing the Congress’s intention appears to be that cities that have incurred high debts may have to make do with lower service levels; losing the freedom to choose low taxes and low service may be a consequence of incurring unsustainable debt and seeking

329. See Joseph Slater, Interest Arbitration as Alternative Dispute Resolution: The History from 1919 to 2011, 28 OHIO ST. J. DISP. RESOL. 387, 400 (2013) (“Approximately thirty states use binding interest arbitration as the final step in public-sector impasse resolutions for at least some public employees.”).

330. Id. at 400 (citing IOWA CODE ANN. § 20.22(9)(c) (West 2010) (specifying “ability of the public employer to finance economic adjustments” as criterion); id. at 403 (citing OHIO REV. CODE ANN. § 4117.14(G)(7)(c) (West 2012) (specifying “ability of the public employer to finance and administer the issues proposed” as criterion)); id. at 404 (citing MONT. CODE ANN. § 39-34-103(5)(b) (West 2009) (specifying “financial ability of the public employer to pay” as criterion)).


bankruptcy protection.\(^{333}\)

After the comparison group is assembled, the court would have to compare tax levels across the group, taking account of the fact that there are different taxes that may be set at different levels relative to each other. However, this step of the analysis by using the total amount of money collected as a common basis of comparison. Doing so could render this step of the process as simple as looking at taxes collected as a percentage of tax capacity across the comparison group.\(^{334}\)

The final step in the analysis is to determine whether the debtor’s taxes meet the top-of-the-range criterion. Applying the idea of the top of the range is a quintessential line-drawing exercise, and any effort to define it will be challenged on the ground that the line could have been drawn somewhere else.

One possible specification would be to look to the absolute top of the range; under this specification, the debtor must impose taxes at or higher than the highest rate of any of its peers. This approach yields a determinate standard that plausibly honors congressional intent to require municipalities to do all they reasonably can before receiving federal bankruptcy relief, and it seems to be consistent with how the top-of-the-range criterion has been applied in the limited case law to date. However, the approach is extreme and ignores all peers other than the highest-taxing one.

Another approach would be to require taxation in the top quintile. The quintile has some precedent as a cutoff point in evaluating taxes,\(^{335}\) and the quintile approach may not allow a single peer to set taxes, depending on the number of peers.

A third approach would be to interpret the top of the range as the top half of the range; above-median taxes would be enough to qualify the debtor for bankruptcy relief. This standard is determinate and represents defensible line-drawing—if the debtor is not in the top half of the cities, it probably is not at the top of the range. On the other hand, it may not

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333. It seems that a municipality should be excluded from the debtor’s comparison group if the municipality is itself insolvent or in financial distress. Also, if the top of the range puts taxes so high relative to service levels that revenue will actually decrease because of noncompliance or declines in property values or population, the municipality should be able to make that argument. The top-of-the-range criterion would apply only to tax rates that are on the upward slope of the revenue hill.


335. Zhao, supra note 326, at 8, 12–13 (analyzing tax capacity by quintile and in particular comparing top and bottom quintiles).
ask enough of the debtor to meet congressional intent.

Finally, the court could allow the comparison group itself to determine what “top of the range” means in the particular context. A plot of the comparison group’s tax rates on a histogram might yield an obvious gap between the top and the rest of the range, but this approach probably will not always work, depending on the data. Cluster analysis, a field of study prominent in artificial intelligence research, offers a more formal version of this approach. This field uses algorithms that “separate a finite, unlabeled data set into a finite and discrete set of ‘natural,’ hidden data structures.”336 Thus, it seems that cluster analysis theoretically could be used not just to determine what cities constitute the top group in a range, but also to determine the comparable group itself. Where this approach will work, with or without formal cluster analysis, it appears preferable due to the fact that it takes advantage of the data that is actually before the court.

The top-of-the-range criterion respects congressional intent to require some degree of sacrifice in the form of taxation before granting bankruptcy relief. It is less extreme and arguably more realistic than the top-of-the-hill criterion; after all, it requires only that the city charge taxes at the same level that some of its peers are already charging. The top-of-the-range criterion does not perfectly capture the idea that a municipality should not be able to spend itself into insolvency deliberately in order to avoid its debts, but the criterion makes such a strategy considerably less attractive because a city employing the strategy would have to charge comparatively high taxes as part of its bankruptcy.

The top-of-the-range criterion probably is also easier to apply than the top-of-the-hill criterion. The two criteria seem equally easy to articulate and to understand conceptually, but applying the top-of-the-hill criterion necessarily involves a hypothetical exercise in determining what would happen if tax rates were increased, while the top-of-the-range criterion could entail only a comparison of actual tax levels across cities. The top-of-the-range criterion is arguably more workable than the top-of-the-hill criterion and more determinate than the share-some-pain criterion. The top-of-the-range criterion is a plausible way of implementing Congress’s will, especially when incorporated into a framework that uses the other criteria as well.

4. Combining the Criteria

As noted previously, this Article suggests that a municipality should tax to the top of the range, both at the eligibility stage and the plan confirmation stage, unless it can offer an explanation. Acceptable explanations would include that tax increases would be counterproductive because they would reduce revenue, would be legally forbidden, or would be electorally impossible without bankruptcy. The latter explanation would be accepted only at the confirmation stage.

Taxing to the level of one’s highest-taxing peers seems reasonably calculated to capture the notion of paying “as much as reasonably possible” that comes through in the statutes’ legislative history. The top-of-the-range criterion is probably more workable and is in principle less extreme and therefore more workable than the top-of-the-hill criterion, because it does not require taxation to the utmost extent of revenue-generating capacity. In some cases, however, it will be plausible that raising taxes to the top of the comparable range will be counterproductive—the top of the hill may be reached at a lower tax level than the top of the range. In such cases, the city should be able to tax to the top of the hill. Thus, the framework suggested here contains elements of both the top-of-the-range and the top-of-the-hill tests. Although adding an analysis of the top of the hill to an analysis of the top of the range would sacrifice the judicial economy of using the latter criterion that would happen only in the subset of cases where the top-of-the-hill criterion is questioned.

The Article envisions using the top-of-the-range criterion for both bankruptcy eligibility and plan confirmation. Judicial precedent supports the notion that taxes are relevant at both stages, and neither the legislative history nor the case law—in most cases—gives a basis for making taxes relevant in different ways at different stages. Stockton is the exception; it suggests that the tax criterion should not be applied at the eligibility stage when bankruptcy is what will make tax increases feasible. This Article suggests that municipalities should be able to make the “Stockton argument,” and its framework thus can be seen as influenced by the share-some-pain test. The framework suggested in this Article thus synthesizes the three distinct specific ideas about taxes in municipal bankruptcy that can be discerned from the legislative history and case law.

There is no clear congressional command that inescapably compels the use of any specific test or framework to give shape to the idea that taxes are relevant; the open-ended municipal bankruptcy statute reflects an idea about taxes that, though unmistakably and consistently present, was vaguely expressed. Thus, filling the gap between the vague direction
the statute provides and a workable standard necessarily entails adding substance, and the result can always be challenged. But fidelity to congressional intent requires the effort to establish some workable standard, imperfect though the result will be. This Article has presented such a standard.

CONCLUSION

Congress intended to limit bankruptcy relief to municipalities that cannot reasonably meet their obligations, and it intended for bankruptcy courts to consider tax levels in making that determination. No one section of the statute expressly makes tax levels relevant; instead, courts have found the idea inherent in four different statutory provisions. Thus, although the case that taxes are relevant is solid, how exactly they are relevant is unclear. This Article advances the discussion on just how taxes have to be before a municipality is eligible for bankruptcy and can have a plan confirmed. The Article has suggested that courts should first ask whether a municipality is taxing as high as its peers. If the debtor is not taxing at that level, it should be allowed to explain why not: perhaps doing so is legally impossible or economically infeasible, or perhaps bankruptcy will itself be a way of obtaining more revenue. Congress did not state its intention precisely, so no specific relationship between tax levels and municipal bankruptcy is plainly compelled by the statute, but this Article has argued that a combination of the three criteria suggested in the case law—top-of-the-hill, share-some-pain, and top-of-the-range—is a pragmatic way of carrying out Congress’s command.