Bond Case Briefs

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NYT: Pension Funds Wary as Bankrupt City Goes to Trial.

Wall Street is taking America's biggest pension fund to court this week, for a long-awaited battle over who takes the losses when a city goes bust — workers and retirees, municipal bondholders, or both.

Stockton, Calif., declared Chapter 9 bankruptcy last year after suffering one of the country's sharpest riches-to-rags swings when the mortgage bubble burst. Struggling to stay afloat, Stockton has slashed tens of millions of dollars' worth of city services — firefighters, senior centers, library programs for at-risk children — and said it would cut its municipal bond repayments to a degree never seen before in a municipal bankruptcy.

But it has drawn the line at slowing down its current workers' pension accrual, or cutting the benefits its retirees now receive.

Mutual funds that hold the threatened bonds, and the insurers that guarantee them, have cried foul, citing the principle that in bankruptcy, similar classes of creditors must be treated the same way. Their objections have prompted the federal bankruptcy judge handling Stockton's case, Christopher M. Klein, to schedule a four-day trial this week, starting Monday.

The immediate question before the judge is whether Stockton qualifies for Chapter 9 at all; unlike companies, cities must meet certain criteria before they can get federal court protection from creditors.

But there is a looming, larger question that has pension funds around the country nervous: Will a victory by bondholders in Stockton pave the way for cuts in its workers' pensions and its payments to Calpers, which, in turn, could lead to the demise of other public pension plans?