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Illinois Lawmakers Propose Easier Path to Municipal Bankruptcy.

(Reuters) - Lawmakers in financially strapped Illinois have introduced a bill that would make it easier for the state's many struggling local governments to file for Chapter 9 bankruptcy, and they have support from the newly elected governor.

Bill co-sponsor Representative Joe Sosnowski said municipalities should have more options for repairing their finances, including seeking protection from creditors without the state's approval as currently required.

"You don't want to make it too easy and you don't want to make it near impossible," the Republican from Rockford said. "The problem now is it's near impossible."

House Bill 298, now before the House rules committee, proposes that "any municipality may file a petition and exercise powers pursuant to applicable federal bankruptcy law."

Governor Bruce Rauner, who entered office in January, is lending his support. He is "committed to turning around Illinois - that includes providing relief to communities that are struggling," his office said in an email to Reuters.

Illinois has the lowest credit rating of any state, and the bill may shield the state from the financial woes of local governments by allowing them to file for bankruptcy.

"I believe municipalities are going to be left more and more to their own devices," said Republican Rep. Ron Sandack of Downers Grove, the bill's sponsor. "We ought to give them all of the financial tools they can have to handle their own affairs."

Local governments in Illinois, with the exception of the Illinois Power Agency, currently may not voluntarily petition for Chapter 9 protection without specific authority from the state. Supporters of HB 298 describe that process as convoluted.

Karol Denniston, a partner at Squire Patton Boggs, cautioned that Illinois should also look to follow the example of states with programs for intervening when local finances fall on hard times to help avert bankruptcy filings.

"How do you make sure the process isn't chaotic?" said Denniston, who helped draft rules for guiding Chapter 9 filings in California. "If you're going to say, 'Have at it,' impose some oversight and discipline."

Michigan appoints emergency managers with the power to restructure finances and modify and renegotiate contracts for local governments. They may also file Chapter 9 petitions, with the governor's approval, as Detroit did due to its overwhelming financial problems.

Some see House Bill 298 being more about giving local officials leverage in labor talks over pensions after judges in the bankruptcy cases of Stockton, California, and Detroit said pensions may be impaired in Chapter 9.

“Chapter 9 gives you the negotiating benefit of saying ‘we want to make these changes – or else,’” said municipal bankruptcy expert James Spiotto of Chapman Strategic Advisors.

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