

CHAPTER 9

Chapter 9 is a rarely used and specialized chapter of the Bankruptcy Code providing for reorganization of municipalities. The term “municipalities” is defined broadly to include many different types of “political subdivision or public agency or instrumentality of a state” which could include cities, towns, counties, taxing districts, special districts, municipal utilities, school districts and hospital districts.

Chapter 9 was originally enacted in 1934 in response to hundreds of municipal bond defaults in the 1930’s. Since 1934, there have been only approximately 500 chapter 9 cases in the entire United States. The last 3 years have seen a significant uptick in filings. Municipal debt defaults are only one reason for current filings, many of which have been caused by other reasons including large judgments, labor costs, pension obligations, lower general revenues, and hospital bonds or operating expenses of a health system.

Kentucky is one of 26 states which permits a chapter 9 filing. KRS 66.400 provides that any taxing agency or instrumentality as defined in chapter 9 of the Bankruptcy Code may file a petition. A “county” cannot file a petition unless its proposed plan is first approved by the state local debt officer (although not defined within the statute, this should currently be the Governor’s Department for Local Government. Tony Wilder from Boyle County is the current Commissioner). Thus, for a county to file chapter 9, more significant state government oversight will be required than for a non- county entity.

There are some similarities but many differences between chapter 9 and chapter 11. If a Kentucky municipality or instrumentality were to file chapter 9, the Chief Circuit Judge of the Sixth Circuit would name the bankruptcy judge to handle the case, and it is not required to be the bankruptcy judge sitting in the same district as the debtor. Likewise, it is possible that a

Kentucky bankruptcy judge could be appointed to handle a municipal bankruptcy in another state. Often times, bankruptcy judges have been appointed from neighboring states to avoid appearances of political persuasion, since the chapter 9 process is fraught with highly – charged political issues. Other common issues include disputes over eligibility to file, proving insolvency, and the municipalities’ “good faith” efforts to first negotiate with its creditors prior to filing.

No attorney in the Commonwealth of Kentucky has handled a chapter 9 case as of yet. DelCotto Law Group has extensive information ready and waiting, as we do anticipate the issues in chapter 9 will hit the Commonwealth sooner rather than later, be that by way of a Kentucky filing or the appointment of a Kentucky judge to another state’s filing. As with all its cases, DLG believes in analyzing not only the possibility of actually filing chapter 9, but also the pros and cons of working with all the constituents to avoid chapter 9; the advantages and disadvantages of the numerous issues that will arise in a chapter 9 filing (in comparison and contrast to chapter 11 cases); and the importance of the negotiation process before, during, and after such a filing.

DelCotto Law Group is prepared to assist those involved in a municipality fiscal crisis to balance the interests of all parties concerned in order to maximize the situation.