

## TO DISAPPEAR A CITY

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*For all the remedies that have been proposed for cities in distress, what has yet to be proposed is to make a city disappear. This Article explores such a proposal. Specifically, the Article will entertain the idea that a combination of Chapter 9 bankruptcy and disincorporation can be used to address municipal insolvency.*

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### INTRODUCTION

In the October 1995 issue of *The Atlantic*, Witold Rybczynski identified *the* problem for a city in decline:

[A]lthough a city is often said to be shrinking, its physical area remains the same. The same number of streets must be policed and repaired, sewers and water lines maintained, and transit systems operated. With fewer taxpayers, revenues are lower, often leading to higher taxes per capita, an overall deterioration of services, or both. More people depart, and the downward spiral continues.<sup>1</sup>

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1. Witold Rybczynski, *Downsizing Cities*, *The Atlantic* (Oct. 1995), <https://www.theatlantic.com/magazine/archive/1995/10/downsizing-cities/308395/>.

He remarked, “Downsizing has affected private institutions, public agencies, and the military, as well as businesses,” and asked, “Why not cities?”<sup>2</sup> His question has become more relevant in the aftermath of the Great Recession. Cities and towns that once served many citizens in their industrial heydays now serve far fewer people and strain to afford services for those that remain.<sup>3</sup>

Under most assumptions, cities, towns, and other municipalities are expected to exist in perpetuity, except, some company towns—fiefdoms whose castle, heavy industry, has since crumbled—have lost their purpose.<sup>4</sup> State lawmakers can respond to municipal insolvency in many ways: bailout, disincorporation, receivership, bankruptcy, and indifference.<sup>5</sup> This Article entertains the idea that a combination of Chapter 9 bankruptcy and disincorporation may be used to address municipal insolvency.

Part I of this Article discusses the form and function of municipalities in the United States, and better yet, attempts to quickly explain why those forms and functions exist in the first place. Part II reviews the methods by which municipalities may adjust debt in cases of insolvency. Part III uses private companies to illustrate the distinction between economic distress and financial distress, and how that distinction relates to municipalities and the policy rationale for municipal debt adjustment in Bankruptcy Court. Part IV discusses how, and under what circumstances, a municipality may be disincorporated or otherwise destroyed. In conclusion, part V applies the theory of Chapter 9 bankruptcy and disincorporation as a solution to municipal insolvency to the city of Hamtramck, Michigan. In the end, lawmakers, bondholders, and citizens should be able to evaluate the idea and understand what it does and does not achieve.

## I. LOCAL GOVERNMENT IN THE UNITED STATES

Ninety thousand and fifty-six municipalities—counties, cities, towns, school districts, water and sewer districts, and development authorities—are said to scatter the realm.<sup>6</sup> Ever since Captain Thomas Hutchins, an engineer for the Royal American or 60th Regiment of Foot

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2. *Id.*

3. *See* Michelle Wilde Anderson, *The New Minimal Cities*, 123 *Yale L.J.* 1118, 1122, 1130 (2014).

4. *See id.* at 1120.

5. *See id.* at 1155.

6. Carma Hogue, U.S. Census Bureau, *Government Organization Summary Report: 2012*, at 1 (2013), <https://www.census.gov/content/dam/Census/library/publications/2013/econ/g12-cg-org.pdf>.

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of the British Army, established a system of land division in 1765, Great Lakes states in particular have been stuck with a fractured system of local democracies.<sup>7</sup> The system, articulated in the appendix of the *Journal of a March from Fort Pitt to Venango and from Thence to Presqu'Isle* in 1765, specified as follows:

Lay out upon a river or creek if it can be found conveniently, a Square of 1,760 yards or a mile on each side, which will contain 640 acres.

Around the town (stockade fort) are the commons of three miles square, containing exclusive of the lots above mentioned 5,128 acres. On three sides of the town five (5) other squares will be laid out, of three (3) square miles containing 5,760 acres each.

The entire tract for each fort forms a township six miles wide and nine miles long and all sub-divisions are to be squares and all the lines are to be parallel.<sup>8</sup>

On May 20, 1785, the Continental Congress codified Captain Hutchins's proposal in the Land Ordinance of 1785 that determined how to settle the Northwest Territory.<sup>9</sup> The Northwest Territory would later become Indiana, Illinois, Minnesota, Michigan, Ohio, and Wisconsin.<sup>10</sup>

Originally set up as federal divisions of land for sale to future settlers, these townships became functional municipalities that provided their residents with political dominion.<sup>11</sup> States in the Midwest and Northeast developed in such a way that a multiplicity of municipalities came into existence over time.<sup>12</sup> Comparatively, vast open spaces and unincorporated territory define the development of the South and West.<sup>13</sup> For example, Ohio has 2,245 municipalities, 668 school districts, 841 special districts,<sup>14</sup> and a population of approximately 11.7 million.<sup>15</sup> Georgia has 535 municipalities, 180 independent school districts, 510

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7. David Rusk, Changing the "Rules of the Game": Tools to Revive Michigan's Fractured Metropolitan Regions, 13 J. L. Soc'y 197, 202–03 (2011).

8. *Id.* at 203.

9. *Id.* at 204.

10. *Id.*

11. *Id.* at 206–07.

12. *See* Rusk, *supra* note 7, at 210–11.

13. *See id.* at 211–12.

14. *Local Governments by Type and State: 2012*, U.S. CENSUS BUREAU, <https://factfinder.census.gov/bkmk/table/1.0/en/COG/2012/ORG02.US01> (last visited Oct. 14, 2018).

15. *QuickFacts Ohio*, U.S. CENSUS BUREAU, <https://www.census.gov/quickfacts/fact/table/oh> (last visited Oct. 14, 2018).

special districts,<sup>16</sup> and approximately 10.4 million people.<sup>17</sup> Each municipality is a political dominion that both elected leaders and citizens have been reluctant to relinquish.

Governmental units come in an assortment of shapes and sizes with an assortment of powers and responsibilities.<sup>18</sup> School districts provide education. Water and sewer districts provide potable water and waste disposal. Counties, cities, and towns provide a broad array of services, such as police and fire safety, parks and recreation, and trash removal.<sup>19</sup> More often than not, the myriad of functions municipalities perform are paid for by taxes on the income, property, and purchases of the people who reside within the municipal unit's jurisdictional boundaries, and transfers from the states and Federal Government.<sup>20</sup>

To carry out their functions, municipalities contract and hire public employees to provide services and sometimes promise those employees deferred compensation in the form of public pensions.<sup>21</sup> Municipalities also access capital markets and issue debt with municipal bonds to pay for the construction of schools, parks, jails, and other capital projects.<sup>22</sup> Just in 2017, \$453.5 billion in municipal bonds were issued.<sup>23</sup> At times, the costs to service those debts and meet those promises becomes insurmountable. Municipalities may become so insolvent and so unable to render public services that the social contract is subverted—as it was in the city of Detroit when prior to bankruptcy in 2013, residents could expect to wait over an hour for help to arrive after they called 911.<sup>24</sup> In most

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16. *Local Governments by Type and State: 2012*, *supra* note 14.

17. *QuickFacts Georgia*, U.S. CENSUS BUREAU, <https://www.census.gov/quick-facts/fact/table/ga> (last visited Oct. 14, 2018).

18. Fred L. Morrison, *The Insolvency of Public Entities in the United States*, 50 AM. J. COMP. L. 567, 567–68 (2002).

19. *Id.* at 568.

20. *Tax Policy Center Briefing Book: State (and Local) Taxes*, TAX POL'Y CTR., <https://www.taxpolicycenter.org/briefing-book/what-are-sources-revenue-state-governments> (last visited Oct. 14, 2018).

21. See, e.g., Mary Williams Walsh, *A \$76,000 Monthly Pension: Why States and Cities Are Short on Cash*, N.Y. TIMES (Apr. 14, 2018), <https://www.nytimes.com/2018/04/14/business/pension-finance-oregon.html> (discussing Oregon's mounting pension obligations resulting from the retirement of public employees hired in the 1980s and 1990s).

22. See Morrison, *supra* note 18, at 568–70.

23. Laila Kearney, *Trailing Deal Surge, Muni Market Heads into 2018 on Waning Supply*, REUTERS (Dec. 29, 2017, 3:05 PM), <https://www.reuters.com/article/usa-municipals-deals/trailing-deal-surge-muni-market-heads-into-2018-on-waning-supply-idUSL1N1OT0UN>.

24. Anderson, *supra* note 3, at 1120, 1199 n.313; Monica Davey, *Financial Crisis Just a Symptom of Detroit's Woes*, N.Y. TIMES (July 8, 2013), <https://www.nytimes.com/2013/07/09/us/financial-crisis-just-a-symptom-of-detroits-woes.html>.

cases, cutting spending and raising taxes can remedy insolvency, however, in rare cases, it cannot.<sup>25</sup> In those latter extreme cases, states—to which municipalities are merely children—can order that democracy be canceled, if only temporarily, that the municipal charter be ripped up, or that debt be adjusted in Bankruptcy Court.<sup>26</sup>

## II. CHAPTER 9 BANKRUPTCY

In the 1930s, an estimated 4,770 municipalities defaulted on their debt.<sup>27</sup> Unable to compel creditors to participate in debt adjustment, these defaults were disorderly.<sup>28</sup> Debt adjustment required the consent of one hundred percent of creditors—an impossible hurdle.<sup>29</sup> Rarely could all creditors be notified of a case, and those that could had an incentive to individually adjudicate their claims.<sup>30</sup> By that process, “a race to the courthouse,” the first to sue the municipal debtor and obtain a writ of mandamus (i.e., a court order to raise taxes), often saw the best recovery.<sup>31</sup> Unfortunately, this did not address the total debt burden, which left other creditors without recourse and some communities with confiscatory levels of taxation.<sup>32</sup> Often, both the municipal debtor and creditors were left unsatisfied.

On the matter of municipal insolvency, state law was, and still is, impotent.<sup>33</sup> The Constitution’s Contract Clause impedes the ability of states and municipalities to impair contracts.<sup>34</sup> The Federal Government however, under Article I, section 8 of the Constitution, has the power to “establish . . . uniform Laws on the subject of Bankruptcies,” or, in other words, impair contracts.<sup>35</sup> Chapter 9 was introduced to Title 11 of the United States Code (i.e., Bankruptcy Code) in 1934.<sup>36</sup> The law ended the

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25. See Omer Kimhi, *Reviving Cities: Legal Remedies to Municipal Financial Crises*, 88 B.U. L. REV. 633, 656–58 (2008).

26. See Michelle Wilde Anderson, *Dissolving Cities*, 121 YALE L.J. 1364, 1386, 1403–04 (2012); Anderson, *supra* note 3, at 1190.

27. George H. Hempel, *An Evaluation of Municipal “Bankruptcy” Laws and Procedures*, 28 J. FIN. 1339, 1340 (1973).

28. *Id.*

29. *Id.*

30. *See id.*

31. *See id.*; *Race to the Courthouse*, BLACK’S LAW DICTIONARY (10th ed. 2014).

32. See Clayton P. Gillette, *Bondholders and Financially Stressed Municipalities*, 39 FORDHAM URB. L.J. 639, 644 (2012).

33. See ROBERT S. AMDURSKY ET AL., MUNICIPAL DEBT FINANCE LAW 418 (2d ed. 2013) (discussing the failures of the state legislature in dealing with municipal insolvency).

34. U.S. CONST. art. I, § X, cl. 1.

35. U.S. CONST. art. I, § VIII, cl. 4.

36. Municipal Bankruptcy Act, ch. 345, 48 Stat. 798 (1934) (repealed 1978) (creating Chapter IX of the Bankruptcy Act of 1898).

incentive to “race to the courthouse” and the ability for a minority of creditors to upend otherwise consensual settlements.<sup>37</sup> Notably, the Supreme Court invalidated Chapter 9 in 1936 in *Ashton v. Cameron County Water Improvement District*.<sup>38</sup> Two years later, after the Supreme Court acquired two new members and a second law was enacted (1937),<sup>39</sup> the Supreme Court overturned its earlier decision in *United States v. Belkins*.<sup>40</sup> Since then, Congress has amended Chapter 9 multiple times.<sup>41</sup> Each time the law was amended—in 1976,<sup>42</sup> 1978,<sup>43</sup> 1984,<sup>44</sup> 1988,<sup>45</sup> 2005,<sup>46</sup> and 2010<sup>47</sup>—it became more like Chapter 11 (the section of the Bankruptcy Code that applies to commercial debtors).<sup>48</sup>

For decades, Chapter 9 bankruptcy went untested. Special districts (water and sewer districts, development authorities, public utilities, etc.) used it, but no major cities filed for bankruptcy. New York City teetered on the brink of insolvency in the 1970s but was saved via state intervention and a federal bailout President Gerald Ford authorized.<sup>49</sup> Finally, Orange County, California, filed for bankruptcy in 1994, but that case did

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37. See Hempel, *supra* note 27, at 1340–41.

38. See 298 U.S. 513, 532, 534 (1936) (holding the Municipal Bankruptcy Act, which permitted local governmental units to voluntarily attain bankruptcy relief, unconstitutionally interfered with state sovereignty), *superseded by statute*, Act of Aug. 16, 1937, ch. 657, 50 Stat. 653, *as recognized in* *United States v. Belkins*, 304 U.S. 27 (1938); *Justices 1789 to Present*, SUP. CT. U.S., [https://www.supremecourt.gov/about/members\\_text.aspx](https://www.supremecourt.gov/about/members_text.aspx) (last visited Oct. 14, 2018).

39. See Act of Aug. 16, 1937, ch. 657, 50 Stat. 653 (creating Chapter X of the Bankruptcy Act of 1898, which was later re-designated as Chapter IX); Hempel, *supra* note 27, at 1341.

40. See 304 U.S. at 50–51, 54 (upholding the provision allowing state taxing officials to work with creditors).

41. See 11 U.S.C. §§ 901–46 (2012).

42. Chapter IX of the Bankruptcy Act of 1898, as amended in 1937, went largely unchanged until it was amended again in 1976 in response to New York City’s financial crisis. See Act of Apr. 8, 1976, Pub. L. No. 94-260, 90 Stat. 315.

43. The earlier 1976 revisions were adopted nearly identically into the 1978 Bankruptcy Code as Chapter 9. See Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, § 101, 92 Stat. 2549, 2621–25 (codified as amended at 11 U.S.C. §§ 901–46).

44. Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, 98 Stat. 333 (codified as amended in scattered sections of 11 U.S.C.).

45. Act of Nov. 3, 1988, Pub. L. No. 100-597, 102 Stat. 3028 (codified as amended in scattered sections of 11 U.S.C.).

46. Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, 119 Stat. 23 (codified as amended in scattered sections of 11 U.S.C.).

47. Bankruptcy Technical Corrections Act of 2010, Pub. L. No. 111-327, 124 Stat. 3557 (codified as amended in scattered sections of 11 U.S.C.).

48. See AMDURSKY ET AL., *supra* note 33 (discussing the adoption of Chapter 11’s terminology and definitions).

49. See RICHARD RAVITCH, *SO MUCH TO DO: A FULL LIFE OF BUSINESS, POLITICS, AND CONFRONTING FISCAL CRISES* 85–86, 96 (2014).

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little to demystify Chapter 9.<sup>50</sup> Only in the Great Recession has the architecture created under the second law enacted in 1937, and later amendments, been tested. Vallejo, California, filed in 2008.<sup>51</sup> Prichard, Alabama, filed in 2009.<sup>52</sup> Central Falls, Rhode Island, filed in 2011.<sup>53</sup> Jefferson County, Alabama, filed in 2011.<sup>54</sup> Stockton, California, filed in 2012.<sup>55</sup> San Bernardino, California, filed in 2012.<sup>56</sup> Detroit, Michigan, filed in 2013.<sup>57</sup>

To file for Chapter 9 bankruptcy, a debtor must attest that it:

(1) is a municipality;

(2) is specifically authorized, in its capacity as a municipality or by name, to be a debtor under such chapter by State law, or by a governmental officer or organization empowered by State law to authorize such entity to be a debtor under such chapter;

(3) is insolvent;

(4) desires to effect a plan to adjust such debts; and

(5)(A) has obtained the agreement of creditors holding at least a majority in amount of the claims of each class that such entity intends to impair under a plan in a case under such chapter;

(B) has negotiated in good faith with creditors and has failed to obtain the agreement of creditors holding at least a majority in amount of the claims of each class that such entity intends to impair under a plan in a case under such chapter;

(C) is unable to negotiate with creditors because such negotiation is impracticable; or

(D) reasonably believes that a creditor may attempt to obtain a transfer that is avoidable under section 547 of this title.<sup>58</sup>

The phrase “specifically authorized” is important.<sup>59</sup> In its first incarnation, the Supreme Court invalidated Chapter 9 because it was believed that to address municipal insolvency in Bankruptcy Court, under federal law, was an affront to state authority.<sup>60</sup> Since then, amendments to the

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50. *In re* Cty. of Orange, 183 B.R. 594, 596 (Bankr. C.D. Cal. 1995).

51. *In re* City of Vallejo, 408 B.R. 280, 288 (B.A.P. 9th Cir. 2009).

52. *In re* City of Prichard, 2011 U.S. Dist. LEXIS 68747, at \*1 (S.D. Ala. 2011).

53. *In re* City of Cent. Falls, 2011 Bankr. LEXIS 5432, at \*2 (Bankr. R.I. 2011).

54. *In re* Jefferson Cty., 474 B.R. 228, 236 (Bankr. N.D. Ala. 2012).

55. *In re* City of Stockton, 493 B.R. 772, 783 (Bankr. E.D. Cal. 2013).

56. *In re* City of San Bernardino, Cal., 499 B.R. 776, 780 (Bankr. C.D. Cal. 2013).

57. *In re* City of Detroit, 501 B.R. 702, 705 (Bankr. E.D. Mich. 2013).

58. 11 U.S.C. § 109(c) (2012).

59. *See id.* § 109(c)(2).

60. *See* Hempel, *supra* note 27, at 1340–41.

law have made the level of permission needed to file a case stricter.<sup>61</sup> Approximately half the states confer to their municipalities the ability to file for Chapter 9 bankruptcy.<sup>62</sup> The state authorization requirement is the first way that consideration of the Tenth Amendment, the separation of powers between the states and Federal Government,<sup>63</sup> is expressed in Chapter 9.

The second expression of the Tenth Amendment in the structure of Chapter 9 is the limited role of the federal bankruptcy judge. Primarily, the role of the federal bankruptcy judge in Chapter 9 is to referee creditor's claims, and after a majority of creditors have consented to a financial settlement, to either confirm the municipal debtor's plan of adjustment or dismiss the case.<sup>64</sup> Any attempts to intervene more directly into day-to-day operations, or the ability of the municipal debtor to sell or use assets, are stymied.<sup>65</sup> Specifically, § 904 of the Bankruptcy Code says:

Notwithstanding any power of the court, unless the debtor consents or the plan so provides, the court may not, by any stay, order, or decree, in the case or otherwise interfere with—

- (1) any of the political or governmental powers of the debtor;
- (2) any of the property or revenues of the debtor; or
- (3) or the debtor's use or enjoyment of any income-producing property.<sup>66</sup>

Because of § 904, a federal bankruptcy judge cannot exercise powers in a Chapter 9 case that he could under other sections of the Bankruptcy Code. For example, in a Chapter 7 or Chapter 11 bankruptcy (for individual or commercial debtors) a bankruptcy trustee would be appointed to administer the estate of the debtor.<sup>67</sup> In Chapter 9, the elected officials retain control of municipal property.<sup>68</sup> Note, the state can exercise external control under § 903.<sup>69</sup> But the state cannot force creditors to accept less than the face value of their claims.<sup>70</sup>

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61. See AMDURSKY ET AL., *supra* note 33, at 421–23.

62. See PEW CHARITABLE TR., THE STATE ROLE IN LOCAL GOVERNMENT FINANCIAL DISTRESS 1, 6–7 (2013), [http://www.pewtrusts.org/~media/assets/2016/04/pew\\_state\\_role\\_in\\_local\\_government\\_financial\\_distress.pdf](http://www.pewtrusts.org/~media/assets/2016/04/pew_state_role_in_local_government_financial_distress.pdf).

63. U.S. Const. amend. X.

64. See PEW CHARITABLE TR., *supra* note 62, at 9.

65. See AMDURSKY ET AL., *supra* note 33, at 436, 439.

66. 11 U.S.C. § 904 (2012).

67. 11 U.S.C. §§ 704(a)(7), 1106(a)(3) (2012).

68. 11 U.S.C. § 903 (2012).

69. *Id.*

70. *Id.* § 903(1); see Hempel, *supra* note 27, at 1344.



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Municipal bankruptcy is peculiar. Claims are bifurcated between secured claims and unsecured claims (i.e., claims backed by collateral and those without collateral) as in any other bankruptcy case, except cities, towns, school districts, etc., do not have shareholders.<sup>71</sup> Moreover, the common interpretation of insolvency does not hold. The common interpretation of insolvency is that liabilities exceed assets.<sup>72</sup> However, because a municipal debtor is not expected to liquidate and recompose itself as a private company would in Chapter 11, whether liabilities exceed assets is irrelevant. Cash flow, specifically whether a municipal debtor can “pay debts as they become due,” is the relevant metric to determine insolvency.<sup>73</sup> Furthermore, a municipal debtor is not required to raise taxes before it files a case.<sup>74</sup>

The ability of creditors to participate is notably diminished from Chapter 11. Under Chapter 11, creditors may submit plans of adjustment (i.e., financial settlement) to compete with the debtor’s plan.<sup>75</sup> Only a municipal debtor can offer a plan of adjustment in a Chapter 9 case.<sup>76</sup> Furthermore, municipal debtors can more easily break labor contracts<sup>77</sup> and can circumvent constitutional and statutory protections for pension benefits.<sup>78</sup>

Once a majority of creditors approve a plan of adjustment, it must be approved by a federal bankruptcy judge.<sup>79</sup> The plan of adjustment cannot unfairly discriminate between creditors, it must be in the best interest of creditors, fair and equitable, and feasible.<sup>80</sup> Public referenda may be required for tax increases or bond issuances that are a part of the plan of adjustment.<sup>81</sup> Save for the ability to impair contracts, the municipal debtor still must follow fiscal rules articulated by state or local law. Note,

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71. 11 U.S.C. § 506(a)(1) (2012); Lotta Moberg & Richard E. Wagner, *Default Without Capital Account: The Economics of Municipal Bankruptcy*, 14 PUB. FIN. & MGMT. 30, 34 (2014).

72. *Insolvent*, MERRIAM WEBSTER, <https://www.merriam-webster.com/dictionary/insolvent> (last visited Oct. 14, 2018).

73. 11 U.S.C. § 101(32) (2012).

74. See Kevin A. Kordana, *Tax Increases in Municipal Bankruptcies*, 83 VA. L. REV. 1035, 1061–62 (1997).

75. 11 U.S.C. § 1121(c) (2012).

76. See 11 U.S.C. § 941 (2012).

77. See *In re City of Vallejo*, 403 B.R. 72, 76 (Bankr. E.D. Cal. 2009) (citing 11 U.S.C. § 901 (2012)).

78. See *In re City of Detroit*, 504 B.R. 191, 194 (Bankr. E.D. Mich. 2013).

79. 11 U.S.C. § 1129 (2012).

80. See AMDURSKY ET AL., *supra* note 33, at 442.

81. See *In re City of Stockton*, 478 B.R. 8, 20 (Bankr. E.D. Cal. 2012) (citing 11 U.S.C. § 941 (2012)).

that should a plan of adjustment meet the cited criteria, a federal bankruptcy judge may approve it without majority consent.<sup>82</sup> Creditors are then bound by the terms of the plan of adjustment.<sup>83</sup> The municipal debtor will then leave Bankruptcy Court with a “fresh start” and is bound to follow the plan of adjustment.<sup>84</sup>

### III. ECONOMIC DISTRESS, INSOLVENCY, AND A “FRESH START”

Because the focus of this Article is the combined impact of Chapter 9 bankruptcy and disincorporation, it is important to entertain critiques of Chapter 9 and emphasize what it does not achieve. Chapters 9 and 11 of the Bankruptcy Code are rehabilitative in their objective.<sup>85</sup> Each is supposed to provide a “fresh start” for the debtor.<sup>86</sup> For a municipality, the theory is that an insurmountable debt can inhibit service delivery as the municipality is forced to dedicate more and more resources to pay off debt rather than for services.<sup>87</sup> Then, the community’s quality of life diminishes, and residents and businesses move away.<sup>88</sup> Taxable value plummets, and the municipality’s ability to service its debt diminishes as well.<sup>89</sup> Finally, there is default.<sup>90</sup> The Bankruptcy Code can make that default orderly and allow for a “fresh start.”<sup>91</sup> Relieved of its debt burden, the municipality can invest in services, and hopefully attract new residents and businesses (i.e., increase taxable value).<sup>92</sup> However, the “fresh start” theory is a response to financial distress, not economic distress.<sup>93</sup>

For private companies, the distinction between financial distress and economic distress can be said to be the difference between an overburdened balance sheet and a bad business model. Financial distress is the inability to match revenues and expenditures, and can be caused by the misallocation of resources.<sup>94</sup> For instance, a company that is otherwise profitable can become unprofitable due to debt service or disruption that

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82. See AMDURSKY ET AL., *supra* note 33, at 444.

83. See *id.* at 441–44.

84. Omer Kimhi, *Chapter 9 of the Bankruptcy Code: A Solution in Search of a Problem*, 27 YALE J. REG. 351, 352–53 (2010).

85. See *id.* at 354; Elizabeth Warren, *Bankruptcy Policy*, 54 U. CHI. L. REV. 775, 798 (1987).

86. Kimhi, *supra* note 84, at 373.

87. See Anderson, *supra* note 26, at 1384.

88. See *id.*

89. See *id.* at 1384–85.

90. See *id.*

91. See *id.* at 1384.

92. See Anderson, *supra* note 26, at 1386.

93. See Kimhi, *supra* note 84, at 374.

94. See *id.*

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causes sales to temporarily fall. Companies that have misallocated resources, but have a sound business model, would file for Chapter 11 bankruptcy.<sup>95</sup> Chapter 11 bankruptcy, on which Chapter 9 is based, would allow a company to liquidate its unprofitable units, adjust debt and re-compose itself.<sup>96</sup> Creditors understand that the commercial debtor would be better off, and their chances for repayment improved, were the commercial debtor to avoid liquidation.<sup>97</sup>

On the other hand, companies that sell an obsolete product or service, and could not be expected to return to profitability even after debt adjustment, would file for Chapter 7 bankruptcy. A liquidation orchestrated under Chapter 7 would see the commercial debtor's assets used to satisfy creditor's claims.<sup>98</sup> Chapter 7 is the Bankruptcy Code's response to companies whose misfortunes are caused by economic distress.<sup>99</sup> For example, Borders Group, former owners of the famed bookstore chain, filed for Chapter 11 bankruptcy on February 16, 2011.<sup>100</sup> The company had \$1.27 billion in total assets, and \$1.29 billion in total liabilities.<sup>101</sup> From the outset, it was believed that Borders Group was economically distressed; that there was a problem with its business model.<sup>102</sup> The use of e-books and competition from online sellers such as Amazon had fundamentally altered demand for bookstores.<sup>103</sup> Later, the company filed a petition for liquidation, or Chapter 7, on July 21, 2011.<sup>104</sup> The company, unable to restructure, closed or sold its 650 stores, laid off 10,700 employees and ceased to operate after October 1, 2011.<sup>105</sup>

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95. See Warren, *supra* note 85, at 787.

96. See Kimhi, *supra* note 84, at 359, 368, 373.

97. Warren, *supra* note 85, at 801.

98. 11 U.S.C. § 726 (2012); see *Chapter 7—Bankruptcy Basics*, U.S. CTS., <http://www.uscourts.gov/services-forms/bankruptcy/bankruptcy-basics/chapter-7-bankruptcy-basics> (last visited Oct. 14, 2018).

99. See 11 U.S.C. § 726; *Chapter 7—Bankruptcy Basics*, *supra* note 98.

100. Aaron Smith, *Borders in Bankruptcy, Will Close 200 Stores*, CNN MONEY (Feb. 16, 2011, 2:22 PM), [https://money.cnn.com/2011/02/16/news/companies/borders\\_bankruptcy/index.htm](https://money.cnn.com/2011/02/16/news/companies/borders_bankruptcy/index.htm).

101. Julie Bosman & Michael J. de la Merced, *Borders Files for Bankruptcy*, N.Y. TIMES (Feb. 16, 2011, 7:25 AM), <https://dealbook.nytimes.com/2011/02/16/borders-files-for-bankruptcy/>.

102. *Id.*

103. Julie Bosman, *The Dog-Eared Paperback, Newly Endangered in an E-Book Age*, N.Y. TIMES (Sept. 2, 2011), <https://www.nytimes.com/2011/09/03/business/media/mass-market-paperbacks-fading-from-shelves.html>.

104. See Michael J. de la Merced & Julie Bosman, *Calling Off Auction, Borders to Liquidate*, N.Y. TIMES (July 18, 2011, 4:57 PM), [https://dealbook.nytimes.com/2011/07/18/borders-calls-off-auction-plans-to-liquidate/?\\_r=0](https://dealbook.nytimes.com/2011/07/18/borders-calls-off-auction-plans-to-liquidate/?_r=0).

105. See *id.*; see also Nathan Bomey, *Barnes & Noble to Shutter Borders' Website*, ANN ARBOR NEWS (Sept. 30, 2011, 2:09 PM), <http://www.annarbor.com/business-review/barnes->

Either because it is uncompetitive or the service or product is obsolete, an economically distressed firm will never make a profit because each year its customer base declines.<sup>106</sup> Like a company whose customer base continues to decline, a municipality whose tax base continues to decline will always be in fiscal crisis.<sup>107</sup> Moreover, cuts in public expenditure alone cannot correct the issue and austerity may hasten the exodus of taxpayers. The Bankruptcy Code may provide the means to adjudicate financial distress but is fundamentally unable to solve economic distress, say some scholars.<sup>108</sup>

The concern then is that even after a successful bankruptcy, where costs have been cut and debt adjusted, the municipality's tax base continues to erode. This concern appears to have been realized in Vallejo, California. The city of Vallejo filed for Chapter 9 bankruptcy in 2008 with \$479 million in total liabilities and completed debt adjustment in 2011.<sup>109</sup> According to *In Vallejo, Bankruptcy Scars Still Visible*, an article the *Wall Street Journal* published a year after the city's case concluded, the city remained poorly positioned.<sup>110</sup> Taxable value has declined by \$1.49 billion since 2008.<sup>111</sup> Expenditures for arts and culture, and parks and recreation have been eliminated.<sup>112</sup> Crime bedevils the ninety-two officers that remain employed from the city's previous police force of 153.<sup>113</sup>

Currently, there is no process to dismantle a municipality in the Bankruptcy Code. Chapter 9 does not contemplate the dissolution of American cities.<sup>114</sup> Modeled after Chapter 11, its objective is rehabilitation.<sup>115</sup> The sections of Chapter 9 that pertain to political control, security

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noble-to-shutter-borders-website/.

106. See Tim C. Opler & Sheridan Titman, *Financial Distress and Corporate Performance*, 49 J. FIN. 1015, 1016 (1994).

107. Kimhi, *supra* note 25, at 640.

108. Kimhi, *supra* note 84, at 380–81.

109. CITY OF VALLEJO, CAL., FIN. DEP'T, COMPREHENSIVE ANNUAL FINANCIAL REPORT FOR THE FISCAL YEAR ENDED JUNE 30, 2012, at vi (2012), <http://www.cityofvallejo.net/common/pages/DisplayFile.aspx?itemId=48546>; Mike Shedlock, *Vallejo Bankruptcy Plan Offers Unsecured Creditors Just 5–20%, as JPMorgan CEO Forecasts More Municipal Bankruptcies*, BUS. INSIDER (Jan. 20, 2011, 2:58 PM), <https://www.businessinsider.com/vallejo-california-plans-to-stick-it-to-its-unsecured-creditors-2011-1>.

110. See Bobby White, *In Vallejo, Bankruptcy Scars Still Visible*, WALL ST. J. (Jan. 19, 2012), <https://www.wsj.com/articles/SB10001424052970204555904577167013455352608>.

111. CITY OF VALLEJO, CAL., FIN. DEP'T, COMPREHENSIVE ANNUAL FINANCIAL REPORT FOR THE FISCAL YEAR ENDED JUNE 30, 2016, at 162 (2016), <http://www.cityofvallejo.net/common/pages/DisplayFile.aspx?itemId=6799801>.

112. Anderson, *supra* note 3, at 1121.

113. Roger Lowenstein, *Broke Town, U.S.A.*, N.Y. TIMES (Mar. 3, 2011), <https://www.nytimes.com/2011/03/06/magazine/06Muni-t.html?mtrref=undefined>.

114. Hempel, *supra* note 27, at 1348.

115. See Clayton P. Gillette & David A. Skeel, Jr., *Governance Reform and the Judicial*

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interest, and insolvency make plain the intent of lawmakers to keep the municipal debtor intact.<sup>116</sup> Chapter 9 does not try to interfere with the municipal debtor's administration, alter its boundaries, or rewrite its charter.<sup>117</sup> Nonetheless, the Bankruptcy Code does not appear to preclude "liquidation" provided there is state authorization and local cooperation.<sup>118</sup>

## IV. DISINCORPORATION

To understand disincorporation, or the death of a municipality, it is important to understand at least a few of the reasons for incorporation, the creation of a municipality. Incorporation has at times been motivated by race, class and desire to hoard tax revenues. For example, particularly at the time of the Great Migration (1910–1970) when black Americans rose from the South to the northern part of the country, white communities could carve out the land occupied by those newcomers.<sup>119</sup> Or, in another scenario, a profitable industry arises, and the immediate residents draw boundaries to sequester the tax revenues from that industry for themselves.<sup>120</sup> Other times, more affluent residents wish to create their own enclave that excludes poorer areas.<sup>121</sup> The hope in the latter example is that the tax burden will be much reduced without the need to offer services such as public transit that affluent residents are less likely to use.<sup>122</sup> In any case, when industries shut down and populations shift, then the purpose of current boundaries is called into question.

Disincorporation is the revocation of a local charter and erasure of boundaries.<sup>123</sup> The process can happen either by public referendum or state decree.<sup>124</sup> In either case, the dissolved territory returns to unincorporated status, or is absorbed into another jurisdiction.<sup>125</sup> The responsibility to render services to citizens becomes some other institution's duty.

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*Role in Municipal Bankruptcy*, 125 YALE L.J. 1150, 1157, 1161 (2016).

116. See Michael W. McConnell & Randal C. Picker, *When Cities Go Broke: A Conceptual Introduction to Municipal Bankruptcy*, 60 U. CHI. L. REV. 425, 470 (1993).

117. See Kimhi, *supra* note 25, at 653.

118. See McConnell & Picker, *supra* note 116, at 482.

119. See Michelle Wilde Anderson, *Cities Inside Out: Race, Poverty, and Exclusion at the Urban Fringe*, 55 UCLA L. REV. 1095, 1103–04 (2008).

120. *Id.* at 1111.

121. See Sam Rosen, *Atlanta's Controversial 'Cityhood' Movement*, THE ATLANTIC (Apr. 26, 2017), <https://www.theatlantic.com/business/archive/2017/04/the-border-battles-of-atlanta/523884/>.

122. See *id.*

123. Anderson, *supra* note 26, at 1367–68.

124. See *id.* at 1375–77.

125. *Id.* at 1367–68.

For unincorporated territory, that duty often falls onto the county.<sup>126</sup> Dissolved territory then shares in the services of the territory into which it is absorbed. Importantly, the limitations of disincorporation as a policy response to financial distress should be noted: disincorporation cannot be used to repudiate debt like Chapter 9 of the Bankruptcy Code.<sup>127</sup>

On more than one occasion, elected leaders have tried to make a municipality and its debt disappear. Alabama dissolved then reconstituted the city of Mobile as the port of Mobile in 1879.<sup>128</sup> The port's borders were redrawn by the State Legislature conveniently to encompass most of the former city's residents and businesses.<sup>129</sup> Even so, state and local officials asserted responsibility to repay debt remained with the defunct city of Mobile.<sup>130</sup> Bondholders sued. The Supreme Court ruled that the state's actions were unconstitutional in *Mobile v. Watson* in 1886.<sup>131</sup> The Supreme Court confirmed the contention of bondholders on two matters; first, that the port of Mobile was liable for the former city's debts, and second, that a writ of mandamus could be enforced upon the new city.<sup>132</sup>

Additionally, the Supreme Court held in *Mt. Pleasant v. Beckwith* in 1879 that “where a municipal corporation is legislated out of existence and its territory annexed to other corporations, the latter, unless the legislature otherwise provides, becomes entitled to all its property and immunities, and severally liable for a proportionate share of all its then subsisting legal debts, and vested with its power to raise revenue wherewith to pay them by levying taxes upon property transferred and the persons residing thereon.”<sup>133</sup> The Supreme Court affirmed the power of states to delineate its powers via instrumentalities (i.e., municipalities) and amend the boundaries and scope of those instrumentalities at will, with exception for where such amendments would impair contracts—a power expressly denied to the states by the Constitution's Contract Clause. Other cases that affirm the limited effect of disincorporation on municipal debt include: *Von Hoffman v. Quincy* (1866),<sup>134</sup> *Broughton v. Pensacola*

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126. *See id.* at 1379.

127. *See id.* at 1384, 1386.

128. *See Mobile v. Watson*, 116 U.S. 289, 299 (1886); Anderson, *supra* note 26, at 1403; *see also* Comment, *Legislative Power over the Contracts of a Municipal Corporation*, 15 YALE L.J. 363, 364–65 (1906) (providing a brief summary of the *Mobile* case).

129. *Mobile*, 116 U.S. at 300.

130. *Id.* at 300–01.

131. *Id.* at 306; *see Gillette, supra* note 32, at 640.

132. *See Mobile*, 116 U.S. at 306; Gillette, *supra* note 32, at 640–41.

133. 100 U.S. 514, 514–20 (1889), Richard W. Flournoy, Jr., *The Rights of Creditors of a Municipal Corporation When the State Has Passed a Law to Abolish or Alter It*, 12 VA. L. REG. 175, 177 (1906).

134. *See, e.g., Von Hoffman v. Quincy*, 71 U.S. 535, 555 (1867).

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(1876),<sup>135</sup> *O'Connor v. City of Memphis* (1879),<sup>136</sup> and *Graham v. Folsom* (1906).<sup>137</sup>

The idea behind disincorporation is that economies of scale can be achieved when layers of public administration are peeled away.<sup>138</sup> The Great Recession and its aftermath have provided further impetus to reduce public expenditures and downsize municipal operations. In an example, common to the Northeast and Midwest, the population of Erie County, New York, has declined by seventeen percent since its peak in 1970.<sup>139</sup> The heavy industry that once employed many left, and so did the people.<sup>140</sup> Yet Erie County still contains the same number of municipalities—forty-four—that it contained in more prosperous times.<sup>141</sup>

Proponents of disincorporation assert that fewer and more sizable jurisdictions can serve citizens better than many scattered municipalities. Moreover, proponents assert that, all else equal, consolidation can save money as the consolidated municipality covers more territory and fixed costs fall.<sup>142</sup> The objective is for the consolidated municipality to deliver the same services to more people, but with less bureaucracy and lower administrative cost. That said, the ability to achieve these economies of scale is unclear from the literature.<sup>143</sup> Such consolidations can be complicated when there are substantive differences in socioeconomic status between two communities that intend to consolidate.<sup>144</sup>

More often, disincorporation is opposed on political rather than financial bases. Citizens value political identity and autonomy in a way that this Article does not seek to quantify. For example, in New Jersey there have been multiple proposals to consolidate its 566 municipalities, 523

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135. See, e.g., 93 U.S. 266, 270 (1876).

136. See, e.g., 74 Tenn. 730, 743 (1881).

137. See, e.g., 200 U.S. 248, 253 (1906).

138. See generally Michael Gaffney & Justin Marlowe, *Fiscal Implications of City-City Consolidations*, 46 ST. & LOC. GOV'T REV. 197 (2014) (finding that consolidation generally does not result in lower taxes and spending).

139. Craig R. Bucki, *Downsizing Done Right: Cutting the Cost of Gov't Through Intermunicipal Collaboration*, 44 URB. LAW 689, 689 (2012).

140. See *id.*

141. See *id.*

142. See Gaffney & Marlowe, *supra* note 138, at 198.

143. See Joseph Martin & Eric A. Scorsone, *Cost Ramifications of Municipal Consolidation: A Comparative Analysis*, 23 J. PUB. BUDGETING ACCT. & FIN. MGMT. 311, 319 (2011).

144. See Eric A. Scorsone, *The Distributional Consequences of Interlocal Agreement Cost Allocation Strategies* 6 (Working Group on Interlocal Servs. Cooperation, Working Paper No. 17, 2006), [https://digitalcommons.wayne.edu/cgi/viewcontent.cgi?referer=https://www.google.com/&httpsredir=1&article=1017&context=interlocal\\_coop](https://digitalcommons.wayne.edu/cgi/viewcontent.cgi?referer=https://www.google.com/&httpsredir=1&article=1017&context=interlocal_coop).

school districts, and 234 special districts.<sup>145</sup> Each time, the State Legislature, which authorizes consolidation, faces fierce opposition from residents.<sup>146</sup> In Michigan, there are 1,773 municipalities, 576 school districts, and 443 special districts.<sup>147</sup> Governor Rick Snyder of Michigan has offered financial incentives for city-to-city and city-to-county consolidation.<sup>148</sup> Few have taken him up on the offer.<sup>149</sup> Governor Andrew Cuomo of New York has called his state's assortment of municipalities "a ramshackle mess."<sup>150</sup> He, too, has offered financial incentives for consolidation among the 1,547 municipalities in New York.<sup>151</sup> Few have taken steps to consolidate.<sup>152</sup> In addition to these examples, the political difficulty of consolidation can be expressed by how few have occurred over the decades. Between 1902 and 2011, an estimated 102 referenda for city and county consolidations have been put to voters, and only twenty-seven have passed.<sup>153</sup>

#### V. HAMTRAMCK, MICHIGAN—BANKRUPTCY AND DISINCORPORATION

"They once called it 'the Wild West of the Middle West,' this 2.09-square-mile island of Slavic zest, an autonomous city surrounded by Detroit, a tight little village where for more than half a century the Polish Americans have loved, hated, worked hard in their yards and on the assembly line, and lived life with gusto," wrote the *New York Times* of Hamtramck, Michigan, in 1974.<sup>154</sup> Three decades later, in 2010, the city, whose population had declined to 22,423 from approximately 26,000 in

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145. *Local Governments by Type and State: 2012*, *supra* note 14; see Jeremy W. Peters, *Lips Move, but No Mergers Result*, N.Y. TIMES (Nov. 18, 2007), <https://www.nytimes.com/2007/11/18/nyregion/nyregionspecial2/18polnj.html>.

146. See Peters, *supra* note 145.

147. *Local Governments by Type and State: 2012*, *supra* note 14.

148. See Kate Linebaugh, *Threats to Town Halls Stir Voter Backlash*, WALL ST. J. (June 8, 2011), <https://www.wsj.com/articles/SB10001424052702304066504576341332888910372>.

149. See *id.*

150. See *id.*

151. See N.Y. DEP'T OF STATE, MUNICIPAL CONSOLIDATION AND EFFICIENCY COMPETITION 2 (2016), <https://www.dos.ny.gov/funding/rfa-16-lge-15/2016%20MCEC%20Guidance%20Document%20.pdf>.

152. See Linebaugh, *supra* note 148.

153. See *id.*

154. William K. Stevens, *Hamtramck Strives to Retain Its Polish Character*, N.Y. TIMES (Oct. 6, 1974), <https://www.nytimes.com/1974/10/06/archives/hamtramck-strives-to-retain-its-polish-character-a-run-on-leeches.html>.



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1974, asked Governor Jennifer Granholm for permission to file for Chapter 9 bankruptcy.<sup>155</sup> She denied the request.<sup>156</sup>

The city's plea was prompted by a tax dispute with the city of Detroit.<sup>157</sup> Prior to the dispute, based on a 1981 accord, Detroit used to send Hamtramck an estimated \$2 million a year in tax revenue from the General Motors Detroit-Hamtramck Assembly Plant that occupied land in both cities.<sup>158</sup> In 2010, Detroit, also financially distressed, claimed it had overpaid for years, and withheld tax revenue from Hamtramck.<sup>159</sup> On March 23, 2011, the two cities settled the dispute.<sup>160</sup> Detroit paid Hamtramck \$3.2 million.<sup>161</sup> However, even with a cash infusion, Hamtramck remained financially distressed.<sup>162</sup> In a report ordered by Governor Rick Snyder (Governor Granholm's successor), the city was shown to have run deficits in 2009, 2010, 2011, and 2012.<sup>163</sup> For example, total revenues in fiscal year 2011 were \$17.3 million and total expenditures were \$17.6 million.<sup>164</sup> In response, the Governor put the city into receivership in 2013 under Public Act 436 of 2012.<sup>165</sup> The city was previously under state control between 2000 and 2007 under Public Act 72 of 1990.<sup>166</sup>

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155. See Kate Linebaugh, *Tax Dispute Squeezes Detroit's Neighbor*, WALL ST. J. (Dec. 20, 2010), <https://www.wsj.com/articles/SB10001424052748703734204576019301978263490>; *QuickFacts Hamtramck City, Michigan*, U.S. CENSUS BUREAU, <https://www.census.gov/quickfacts/fact/table/hamtramckcitymichigan/PST045216> (last visited Oct. 14, 2018).

156. Monica Davey, *Michigan Town is Left Pleading for Bankruptcy*, N.Y. TIMES (Dec. 27, 2010), <https://www.nytimes.com/2010/12/28/us/28city.html>; Jonathan Oosting, *Hamtramck Manager: We'll Pursue Bankruptcy Until 'Door is Shut, Locked, Barricaded, Bolted'*, MICH. LIVE (Dec. 28, 2010), [https://www.mlive.com/news/detroit/index.ssf/2010/12/hamtramck\\_city\\_manager\\_well\\_pu.html](https://www.mlive.com/news/detroit/index.ssf/2010/12/hamtramck_city_manager_well_pu.html).

157. Linebaugh, *supra* note 155.

158. *Id.*

159. *Id.*

160. See Kate Linebaugh, *Hamtramck, Neighboring Detroit Settle Tax Dispute*, WALL ST. J., (Mar. 23, 2011, 4:26 PM), <https://www.wsj.com/articles/SB10001424052748704050204576218843580945066>.

161. *Id.*

162. See HAMTRAMCK FIN. REV. TEAM, REPORT OF HAMTRAMCK FINANCIAL REVIEW TEAM 1 (May 23, 2013), [http://www.michigan.gov/documents/treasury/Hamtramck\\_Review\\_Team\\_Report\\_5-23-13\\_422292\\_7.pdf](http://www.michigan.gov/documents/treasury/Hamtramck_Review_Team_Report_5-23-13_422292_7.pdf).

163. *Id.* at 3.

164. *Id.*

165. *Contract for Emergency Manager Services*, MICH. DEP'T TREASURY 1 (2013), [http://www.michigan.gov/documents/treasury/Hamtramck-EM-Contract-Cathy-Square\\_426238\\_7.pdf](http://www.michigan.gov/documents/treasury/Hamtramck-EM-Contract-Cathy-Square_426238_7.pdf).

166. Press Release, Mich. Dep't of Treasury, Review Team to Examine Hamtramck Finances: Next Step Following Preliminary Review (Apr. 17, 2013), <https://www.crainsdetroit.com/assets/PDF/CD88029417.pdf>; see Anna Fountain Clark &

Hamtramck was also economically distressed. Median household income was only \$23,609,<sup>167</sup> \$27,194 less than the statewide median household income of \$50,803.<sup>168</sup> Over the past decade, the city suffered as much as Detroit from auto plant closures.<sup>169</sup> Another *New York Times* article published in 1979 appeared to capture a history that would repeat itself when it reported “[t]he Chrysler Corporation, on the verge of bankruptcy and pleading for Federal assistance, is closing its Hamtramck assembly plant.”<sup>170</sup> In the Great Recession, Chrysler, LLC, filed for bankruptcy in 2009, as did General Motors.<sup>171</sup> Both companies provided much of the tax revenue for the city and employment for city residents.<sup>172</sup>

For the purposes of this Article, bankruptcy and disincorporation will be considered for Hamtramck instead of the policy of receivership that was implemented by the Governor. This section of the article attempts to answer what happens to the assets and liabilities of erased municipalities. To be sure, this is complicated because only around half the states allow municipalities to file for Chapter 9, and only forty states have statutes in force for disincorporation.<sup>173</sup> Based on those conditions, the theoretical presentation here of bankruptcy and disincorporation is broadly hypothetical. More fundamentally, this research is frustrated by the fact that both Chapter 9 bankruptcy and disincorporation are exceptionally rare.<sup>174</sup> Few municipalities become so indebted as to need the Bankruptcy Code to unwind their debts, and few citizens willfully surrender local autonomy and political identity.<sup>175</sup> Still, this section tries to translate the theoretical into the practical.

Granted permission to file for Chapter 9, Hamtramck would file a

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Evgenia Gorina, *Emergency Financial Management in Small Michigan Cities: Short-Term Fix or Long-Term Sustainability?*, 41 PUB. ADMIN. Q. 532, 534 (2017).

167. *QuickFacts Hamtramck City, Michigan*, U.S. CENSUS BUREAU, <https://www.census.gov/quickfacts/fact/table/hamtramckcitymichigan/PST045216> (last visited Oct. 14, 2018).

168. *QuickFacts Michigan*, U.S. CENSUS BUREAU, <https://www.census.gov/quickfacts/MI> (last visited Oct. 14, 2018).

169. See Linebaugh, *supra* note 155.

170. See William Serrin, *Hamtramck Is Losing a Plant—and More*, N.Y. TIMES, Dec. 16, 1979, at 30.

171. See Bill Vlastic & Nick Bunkley, *Obama Is Upbeat for G.M.'s Future*, N.Y. TIMES (June 1, 2009), <https://www.nytimes.com/2009/06/02/business/02auto.html>.

172. See Linebaugh, *supra* note 155.

173. Anderson, *supra* note 26, at 1376; see PEW CHARITABLE TR., *supra* note 62.

174. *Chapter 9—Bankruptcy Basics*, U.S. COURTS, <http://www.uscourts.gov/services-forms/bankruptcy/bankruptcy-basics/chapter-9-bankruptcy-basics> (last visited Oct. 14, 2018).

175. See *id.*

case, dissolve, and be absorbed into Detroit.<sup>176</sup> Success is incumbent on several steps. First, Hamtramck's plan of adjustment would have to be approved by creditors and a federal bankruptcy judge.<sup>177</sup> Second, approval of the plan of adjustment would depend on local approval of disincorporation.<sup>178</sup> The reason local approval is necessary is that disincorporation would be a formal part of Hamtramck's plan of adjustment.<sup>179</sup> For example, before the city of Stockton could exit bankruptcy, residents had to approve an increase in the sales tax, and those revenues were used to pay creditors.<sup>180</sup> This is in line with Chapter 9's restrictions that a municipal debtor cannot prescribe actions in their plan of adjustment that would otherwise be prohibited (save, of course, for the impairment of contracts).<sup>181</sup> In other words, if disincorporation could only be initiated via public referendum, then such a referendum would have to be held and the motion passed before a municipal debtor could dissolve.

Chapter 9 of the Bankruptcy Code offers debt relief for the soon to be dissolved city. The city of Detroit, which had \$18 billion in total liabilities when it filed for Chapter 9 bankruptcy in 2013, was able to reduce its liabilities by approximately \$7 billion.<sup>182</sup> In lieu of a successful bankruptcy, dissolved territories must account for their debt another way. Most often, a tax district is set up to cover the area of the former city.<sup>183</sup> The former residents pay off the former city's debt.<sup>184</sup> Inside Bankruptcy Court, the city can dispense with liabilities whether they be in the form of bonded debt, leases or other contracts.<sup>185</sup> One unanswered and consequential question is what would happen to liabilities from the former municipality's pension and benefit promises.<sup>186</sup> Certainly, these promises can be reduced in bankruptcy, but it is unlikely that they can be erased entirely.<sup>187</sup> On the other hand, union contracts with current employees would be terminated, as they were when the village of Seneca Falls, New

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176. See 11 U.S.C. § 941 (2012).

177. See 11 U.S.C. § 943(b) (2012).

178. See *id.* § 943(a).

179. See Anderson, *supra* note 26, at 1394.

180. *In re City of Stockton*, 526 B.R. 35, 61–62 (Bankr. E.D. Cal. 2015).

181. See 11 U.S.C. § 943.

182. See Matthew Dolan et al., *Detroit Rising: Life After Bankruptcy*, DETROIT FREE PRESS (Nov. 8, 2015, 8:23 AM), <https://www.freep.com/story/news/local/detroit-reborn/2015/11/08/detroit-rising-life-after-bankruptcy/75085252/>.

183. Anderson, *supra* note 26, at 1386.

184. *Id.*

185. See Hempel, *supra* note 27, at 1344–45.

186. See Anderson, *supra* note 26, at 1383.

187. *In re City of Detroit*, 524 B.R. 147, 211 (Bankr. E.D. Mich. 2014) (quoting 11 U.S.C. § 943(b)(4) (2012)) (citing *In re City of Detroit*, 504 B.R. 97 (Bankr. E.D. Mich. 2013)).

York, dissolved into the town of Seneca Falls in 2012.<sup>188</sup>

In the case of the village of Seneca Falls, the village and town of Seneca Falls went further than state law demanded for the resolution of leftover liabilities. Two different tax assessments were used to separate liabilities related to health care and other post-employment benefits (OPEBs).<sup>189</sup> One assessment was used to pay for health care and OPEBs earned by town retirees who retired prior to the village's dissolution so that former village residents did not pay for those benefits.<sup>190</sup> Another tax assessment was levied upon the property within the former village's boundaries to pay for benefits earned by village retirees and to relieve town residents from that duty.<sup>191</sup> In other words, neither town residents nor former village residents would pay for public servants who never served them.

Even in the event of a successful bankruptcy, a tax district would likely need to be set up to cover the former territory of Hamtramck to pay off any leftover liabilities as was the case in the village of Seneca Falls.<sup>192</sup> But the level of debt under this combined policy could be much reduced—and so therefore the level of taxation to pay off that debt could be much reduced compared to a scenario where a bankruptcy had not occurred and former residents were left with the total debt burden of the former city. For the debt that does remain, it is unlikely that it could be or reasonably expected to be assumed by Detroit (or in the case of a city-to-county consolidation, Wayne County). For example, under consideration in New York is the consolidation of the city of Syracuse and Onondaga County. Current proposals show that the county will assume city services, a new administrative body will be formed, and taxes will be levied, but the accord does not allow the city to transfer any of its liabilities to the new municipality.<sup>193</sup>

Unlike debt, municipal property and other assets owned and earned

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188. See DISSOLUTION COMM. & CGR, VILLAGE OF SENECA FALLS DISSOLUTION PLAN 19 (2009), [https://www.cgr.org/consensuscny/docs/09\\_R-1591\\_SenecaFallsDissolution-Plan.pdf](https://www.cgr.org/consensuscny/docs/09_R-1591_SenecaFallsDissolution-Plan.pdf); David L. Shaw, *Contract Approved for Seneca Falls PD*, FINGER LAKES TIMES (July 9, 2015), [http://www.fltimes.com/news/contract-approved-for-seneca-falls-pd/article\\_ba5f312e-264c-11e5-9ed7-fb975cae9790.html](http://www.fltimes.com/news/contract-approved-for-seneca-falls-pd/article_ba5f312e-264c-11e5-9ed7-fb975cae9790.html).

189. See Telephone Interview with Beverly Warfel, Senior Accountant, Town of Seneca Falls, N.Y. (Aug. 17, 2017).

190. *Id.*

191. *Id.*

192. See DISSOLUTION COMM. & CGR, *supra* note 188, at 1.

193. CONSENSUS, FINAL REPORT OF THE COMMISSION ON LOCAL GOVERNMENT MODERNIZATION 90 (2017), <http://www.ongov.net/shareservicesplan/documents/FinalReport-COMMISSION-FORMAT.pdf>.

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by the dissolved territory would likely be subsumed by Detroit.<sup>194</sup> Cash on hand could be used to settle with creditors, and public assets could be sold and the proceeds used to retire Hamtramck's debts.<sup>195</sup> Specifically, in the context of a Chapter 9 case meant to function like a liquidation, the sale or privatization of public assets is likely to be more feasible.<sup>196</sup> To the extent that public assets would become redundant upon the end of the process, public assets lose their value to the public.<sup>197</sup> Ordinarily in Chapter 9, sale and privatization of assets would be unlikely.<sup>198</sup> For one, Chapter 9 broadly immunizes municipal property from seizure (unless that property has been used as collateral to a debt).<sup>199</sup> Also, because the purpose of Chapter 9 is to leave the debtor intact and still able to deliver services, it would be unwise to auction off property that is useful for service provision.<sup>200</sup>

Ultimately, Hamtramck would cease to exist. The city hall would be auctioned off, so, too, would police cars, administrative offices, and other unneeded municipal property. The former residents of Hamtramck would then vote in the next election as citizens of Detroit.

**CONCLUSION**

Bankruptcy and disincorporation are not presented here as a panacea for municipal insolvency, but rather as a policy process to be considered with other options. So far as disincorporation can erase boundaries, Chapter 9 is useful to do what states and municipalities cannot—impair contracts. On the other hand, insofar as Chapter 9 can reduce debt, disincorporation can amend the municipal debtor's administration, and simplify land use and economic policy to address economic distress.

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194. See McConnell & Picker, *supra* note 116, at 432–33.

195. See Anderson, *supra* note 3, at 1121.

196. See McConnell & Picker, *supra* note 116, at 477.

197. See *id.*

198. See Juliet M. Moringiello, *Decision-Making and the Shaky Property Foundations of Municipal Bankruptcy Law*, 12 BROOK. J. CORP. FIN. & COM. L. 5, 13 (2017).

199. See *id.* at 14.

200. See *id.* at 16.