Statutory Interpretation, Three Ways:
The "Best Interests of Creditors" Test in Chapter 9

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A financially distressed municipality can restructure its debt under Chapter 9 of the Bankruptcy Code over the objection of a creditor only if it can persuade the court that its plan is "in the best interests of creditors."[1] A "best interests" test has been part of our bankruptcy law since the nineteenth century, but what it means in a municipal bankruptcy is unclear. The terrain is not so much contested as it is unexplored.[2] This essay sets out three different ways in which a court might interpret the "best interests" language, each radically different, but all of which can be grounded in the statutory text. The stakes are large, as tens of billions of dollars in municipal debt will likely be restructured over the next decade.[3]

I shall illustrate how the different interpretations play themselves out by exploring the consequences each has for bondholders of the Chicago Public Schools ("CPS") should it file for bankruptcy. As defined in the Bankruptcy Code, "municipality" means any political subdivision, public agency, or instrumentality of the state.[4] Those who live in Chicago find themselves in multiple municipalities within the meaning of Chapter 9 of the Bankruptcy Code. These include the City of Chicago proper, Cook County, the Chicago Park District, and CPS. Property owners in Chicago do

[1] 11 U.S.C. §943(b)(7).

[2] But there are few reported opinions and hardly any at the appellate level. For cases under the 1978 Bankruptcy Code, see In re Mount Carbon Metropolitan District, 242 Bankr. 18 (Bank. Colo. 1999); In re City of Detroit, 524 Bankr. 147 (Bankr. E.D. Mich. 2014); Franklin High Yield Tax-Free Income Fund v. City of Stockton, 542 Bankr. 261 (9th Cir. B.A.P. 2015). The most significant academic commentary is 4 Collier on Bankruptcy ¶943.03[7] (15th ed.).

[3] The restructuring of the debt of Puerto Rico and its municipalities itself involves more than $70 billion debt and the relevant legislation, passed by Congress just last year, uses a variation of the "best interests" test as well.

[4] See 11 U.S.C. §101(40).

not receive a tax bill from CPS directly, but CPS levies taxes that Cook County collects on its behalf.

CPS has annual revenues of about $6 billion.[5] Expenses outpace revenues by hundreds of millions of dollars, and there seems little prospect that this will change. CPS's property tax levies are already at their statutory maximum. A new teachers' contract in late 2017 locked in CPS's obligations to them until 2020, and these costs are themselves 60% of all expenses. Because the number of students is falling, state funding is falling as well. And CPS's operating expenses are not likely to go down much even with a fall in the number of students. Many of CPS's costs are fixed. It costs less to run a high school designed for a thousand students when it is educating only two hundred, but not that much less. The costs of running the physical plant are the same. The administrative structure is the same. The number of teachers can be reduced, but not in proportion to the reduction in the number of students.

The most straightforward way of bringing about operational efficiencies—closing schools—is politically controversial. The underpopulated schools are concentrated in poor neighborhoods on the south and west side of the City. School closings present challenges quite apart from the political firestorms they bring. Among other things, boarded-up schools make blighted neighborhoods worse and consolidating them forces students to cross gang lines on their way to school.

CPS has outstanding debt of $7.5 billion and unfunded pension and retiree liability of more than $10 billion.[6] Without some dramatic change in

[5] CPS receives 28% of its revenues from the state, 55% from local revenues, including property taxes, 15% from federal revenues, and 2% from other sources.

[6] How much more than $10 billion depends on actuarial assumptions and predicting the predicted rate of return on the investment portfolio. For the amount to be as low as $10 billion or even close to it, one needs to accept CPS's prediction that the fund will grow at a rate of 7.75% for decades. This rate of growth seems unreasonably optimistic. Sophisticated investors should enjoy rates of return on their capital that rival whatever CPS can achieve, yet we see such investors willing to accept much less. If J.P.

fortune, there is no chance that CPS will be able to honor these obligations in full. Indeed, even if all of CPS's past debt and unfunded pension obligations were wiped out, it would still lose more than $100 million a year on an operating basis.

CPS can continue to meet operating expenses with additional borrowing, but it is close to losing its ability to borrow on a long-term basis as the interest rate demanded for this debt is close to the statutory cap of 9%. So far, CPS has been able to continue operating through short-term borrowing against future tax revenues and, most recently, against future grants from the state. This source of revenue will be exhausted in this fiscal year or the next. Because CPS has no ability to repay any of the short-term debt, its ability to continue operating also depends on the willingness of holders of existing short-term debt to keep rolling it over.

Without a dramatic increase in state aid or local taxes, CPS's economic collapse is only a matter of time. Over the short-to-medium term, it seems likely that there will be a series of last-minute infusions of cash that do just enough to avert collapse. For a time, the only bright part of the picture was that those overseeing CPS's finances were not the ones who brought it to the brink. They were the equivalent of turn-around specialists in the private sector. They were highly competent, completely aware of the mess in which CPS found itself, and doing everything possible to find a way out of the mess. Unfortunately, a minor misstep by the head of CPS (not being straightforward about some, largely unimportant conflicts among pro-bono legal counsel) led to his departure and a change in the management team. Those now in charge are less experienced and likely less competent.

A Chapter 9 does not follow inevitably if CPS loses the ability to support its ongoing operations. Indeed, a municipality can file a Chapter 9 petition only if the state authorizes it. With minor exceptions, Illinois has not authorized any of its municipalities to file. But state authorization can come quickly in a crisis, and the possibility that CPS will find itself in Chapter 9

Morgan thought it could get a 7.75% return on its capital, it should not be willing to make a 30-year fixed-rate home loan at 4%.

is not at all remote.[7] If CPS does find itself in Chapter 9, much will turn on how the requirement that the restructuring plan is in "the best interest of the creditors" constrains the players, and this question is the focus of this Essay.

Part I explores the interpretation of "best interests" most firmly rooted in history. The "best interests" language first applied to small business bankruptcies in the nineteenth century. An alteration of a creditor's claim in a small business bankruptcy was in the "best interests of creditors" only if the alteration left each individual creditor with at least as much in bankruptcy as she would have received if the bankruptcy had never happened and she resorted to whatever remedies were available under state law.

It is straightforward to apply this idea to municipal debtors. One can argue that, when Congress later incorporated "best interests" language into the first municipal insolvency legislation in the 1930s and again when it codified bankruptcy law in 1978, it did so with an awareness of how "best interests" had come to be understood. When a phrase that has become a term of art is adopted into statutory text, the language should, at least in the absence of strong reasons to the contrary, be interpreted in similar fashion. Under this interpretation of best interests, each creditor of CPS is entitled to however much she would have received outside of bankruptcy if she were left to her own devices.

Part II offers an account of "best interests" that is based on its place in the structure of the statute. When bankruptcy law was codified in the late 1970s, a sharp distinction was introduced between rights that could be asserted by a particular class of creditors on the one hand and rights that a dissenting creditor within a class could assert on the other. Creditors in a

[7] For example, CPS was able to obtain a lower rate of interest on a long-term bond issue last year, one devoted to capital improvements, because it was able to obtain an opinion letter that asserted this particular bond would enjoy special treatment in Chapter 9. See Juan Perez, Jr., Upcoming CPS Bond Issue Gets Favorable Outlook from Wall Street, Chicago Tribune, Dec. 9, 2016. If the interest rate on a bond goes down substantially only because of its special treatment in bankruptcy, the prospect of bankruptcy cannot be that remote.

class can insist on an elaborate hearing in which the bankruptcy judge assesses whether the plan is "fair and equitable" and does not "discriminate unfairly." Each individual creditor, even when the class consents to a particular plan, can insist that the plan be "in the best interests of the creditors."

This structure suggests that "best interests" provides a form of back-up protection of individual creditors when the group votes in a way that is contrary to their interests. The law is structured to encourage classes of creditors to consent to a plan rather than demand a hearing in which it is contested. Such hearings are time-consuming and expensive. It makes sense to avoid such hearings if possible. Bankruptcy law creates an environment that induces parties to look towards a negotiated bargain. If there is sufficient consensus, a class can waive its right to such a hearing.

But dissenting creditors in such a regime need some form of protection. The "best-interest" test ensures that a majority within a class cannot trample on the rights of the minority when it gives up the right to a judicial hearing. Some holding claims in a particular class may not share the same interests as others. Among other things, creditors who dominate a class may hold claims in other classes as well. When they vote in favor of a plan, they may do so because of how another one of their claims is treated under the plan. One can argue that this is the role that "best interests" plays. It serves to protect the minority from a tyranny of the majority.

The judge must ensure that the majority vote fairly reflects the interests of the class as a whole. If there is consensus within a class, the judge no longer needs to engage in a full-blown review of the substantive entitlements of the class. Nevertheless, she must still assess whether the process slighted the rights of the dissenters. Under this interpretation, dissenting CPS bondholders can complain that the plan in not in the best interests of the creditors if the vote somehow does not fairly reflect the interests of everyone in the class, but they would not be able to complain that the plan gave them less than they would have received outside of bankruptcy.

Part III suggests a third interpretation of "best interests." In the case of a financially distressed business, the only stakeholders are investors, and liquidation of the business is an acceptable—indeed, a desirable—option if it provides the stakeholders with the greatest returns. Municipalities are different beasts entirely. Liquidation is generally not an option. The rights of investors need to be weighed against the need to provide essential services to those who live within the municipality. To forge a plan, deals need to be reached with large numbers of diverse constituencies. In any plan, there will be winners and losers among the creditors. The best-interest test gives the judge a final chance to assess how this balance has been struck. Rather than focus on how a particular creditor within a class fares, the best-interest test requires the judge to ask whether the plan gives creditors across all classes the most they can reasonably expect under the circumstances.

In the 1930s, debt came in few flavors. There was often only one class of creditor. If the plan made sense for one creditor, it would make sense for all. Today, municipalities have much more complicated debt structures and, in many cases, the lion's share of the debt is owed, not to holders of financial instruments, but rather to workers and retirees. In the case of CPS, pension and other unfunded obligations are larger, perhaps several times larger, than the institutional debt. Moreover, multiple municipalities compete against the same revenue source. Paying more to CPS creditors necessarily leaves less for creditors of the City of Chicago. Any restructuring will require sorting out how much of the burden the state itself will bear as opposed to local property owners.

In this environment, the judge may need to do more than sit back and let the parties strike a deal or not as they please. If Chapter 9 is to work effectively, one can argue, the judge must take a role in bringing the parties together and putting together a plan that no one likes, but most can live with. In such an environment, the "best interests" test requires the judge to give the plan one final look. It gives a dissenting creditor the right to ask the judge to examine plan one last time and ensure that, after all the other tests have been satisfied, the creditors as a group are being treated as well as can reasonably be expected. The focus is not on the individual creditor, but on creditors as a group.

Each of these three interpretations of "best interests" gives the bankruptcy judge a different role. Under the first, she is a protector of the nonbankruptcy rights of individual creditors. In the second, she is a referee of the bargaining process. She is charged with ensuring that when a class of creditors binds everyone in the class, it respects the rights of the minority.

Under the last interpretation, she is both peacemaker and dealmaker. She is an active player in the process, the person who both forges a consensus among the parties and ensures that the final bargain is a sensible one.[8]

Choosing among these conceptions of "best interests" depends in large measure on some view of what bankruptcy judges are competent to do. More importantly, it may require locating the rule of municipal bankruptcy law within a larger framework of state and local government and who should be fiscally responsible for what. The more responsibility the bankruptcy judge assumes, the lighter the burden that others need to bear.

I. **Origins of Best Interests**

The "best interests of the creditors" test entered bankruptcy law in the 1874 amendments to the short-lived Bankruptcy Act of 1867. These amendments were designed to help facilitate negotiations between trade creditors and their common debtor.

In the late nineteenth century, wholesalers often supplied goods to remote retail merchants on credit. Most would repay them in full, but, as is always the case, some would prove unable to do so. In these cases, the remote suppliers needed to make the best of a bad situation. They had no ability to take over the business of a failed dry goods merchant in some distant city. Nor could they sell the business as a going concern. The business itself had no identity apart from the person who ran it, and that person would not run the business unless she owned it. Sometimes the only sensible path was to force a liquidation of the assets. But liquidations yielded relatively little, and the creditors as a group were open to other options.

In some cases, a retailer would be willing to pay more than the liquidation value of the business if, in exchange, she could keep running it. It might seem that a merchant would not want to pay to continue operating what had been a losing venture, but this was not always the case. Even though the business had lost money in the past, it might make money going forward if it could free itself of past debt. A merchant's inability to pay its

[8] For an excellent discussion of how the judge in the City of Detroit bankruptcy assumed this role, see Melissa B. Jacoby, Federalism Form and Function in the Detroit Bankruptcy, 33 Yale J. Reg. 55 (2016).

suppliers in full might have been caused by a bad harvest that made her own customers unable to pay their bills to her. The merchant might be confident that her customers (and profits) would return with the next good harvest. For this reason, the business had value in her hands over and above its liquidation value even if it had no value in the hands of the suppliers.

In these situations, there was a bargain that could be struck between the suppliers and the merchant that would make both better off. The challenge, however, was getting the creditors to act as one. Without some way to bind dissenting creditors, there was a collective action problem. Each individual creditor had an incentive to engage in hold-up behavior and insist on special treatment as a condition of granting her consent.

The wholesalers had some ability to strike a bargain with the merchant even without a special legal regime. In the early part of the twentieth century, most of those who worked in the credit departments of wholesale suppliers belonged to the National Association of Credit Men. This association set up credit bureaus in major cities. The Credit Men of the suppliers of a struggling merchant in a particular city could ask the local credit bureau to negotiate on their behalf.[9]

But there were limits to what these credit bureaus could do. The local credit bureaus could negotiate with debtors and offer them extensions. It could also oversee a liquidation of the business. But it was hard for the credit bureau to restructure debt. No one wanted to compromise her claim only to see other creditors paid in full.

A "composition," a legal device first developed in England, solved this problem. A statute providing for composition of debts allows a supermajority of creditors to agree to compromise their claims and to bind all, even those who dissent. Such a provision was introduced to American bankruptcy law in 1874. This law soon expired, but it became part of the 1898 Bankruptcy Act, the first long-lived bankruptcy statute in this country.

In addition to requiring a supermajority vote in favor of the compromise with the debtor, the 1874 and 1898 acts also required that the composition

[9] For a discussion of how these credit bureaus operated, see Thomas Clifford Billig, What Price Bankruptcy: A Plea for "Friendly Adjustment," 14 Cornell L. Quarterly 413 (1929).

be in the “best interests of the creditors.” This provision served as a safeguard against the possibility that the composition was not everything it appeared to be. Instead of being put together by someone at the local credit bureau, the composition might be a deal struck between the debtor and some local creditors who were friendly to it.[10] The debtor might then obtain the support of many outside creditors who were naïve or somnolent. The composition, even though a supermajority approved it, might not be a sensible deal that made both the debtor and the creditors better off. The creditors might prefer to be left to their state court remedies. As one court explained:

> If the court is satisfied upon the hearing that the composition offered would pay creditors very considerably less than they might reasonably be expected to realize in the administration of the assets in due course, then the composition is not for the best interest of creditors.[11]

The focus was solidly upon ensuring that the composition did not compromise nonbankruptcy rights. As the Fifth Circuit explained when it struck down a composition a district judge approved:

> the court [below], in becoming satisfied that the offered composition was for the best interests of the creditors, accorded undue weight to the consideration of the anticipated difficulties of enforcing the just claims of creditors, and underestimated the efficiency, under existing conditions, of legal means available to prevent the success of unwarranted obstructive tactics on the part of the debtor.[12]

By the 1930s, the phrase “best interests of the creditors” had long since become “something of a term of art” in the context of the small-business

[10] This appears to have been the case in the classic composition case under the 1898 Act, Fleischmann & Devine v. Saul Wolfson Dry Goods Co., 299 F. 15, 18 (5th Cir. 1924). The lawyer representing the creditor opposing the plan was the head of the local credit bureau and therefore would be unlikely to oppose a plan that the Credit Men supported.

[11] Adler v. Jones, 109 F. 967, 969 (6th Cir. 1901).

[12] See Fleischmann & Devine v. Saul Wolfson Dry Goods Co., 299 F. 15, 18 (5th Cir. 1924).

debtor.[13] The creditors as a group could bind a dissenting creditor only if the deal they struck was giving her more than she could have received if the bankruptcy never happened.

Such a constraint did not undercut the efficacy of the composition. A composition was worth doing only if it yielded more to the creditors than they would enjoy if the firm were liquidated. The composition, like the bankruptcy law of this period, was in the first instance a creditor remedy. Congress enacted the 1898 bankruptcy law (with its provision allowing for composition of debt) only because creditors, including the Credit Men, pushed for it.

The same "best interests" language was made part of the first municipal insolvency statutes, and it is easy to argue that it should have the same meaning in the context of municipal bankruptcy. Just as distant creditors in the nineteenth century needed a way to restructure the obligations owed them by small merchants, holders of municipal bonds had to sort out their rights when their debtor could not pay them.

The first incarnations of municipal bankruptcy statutes were called "compositions." The constitutional justifications put forward for municipal bankruptcy relied in part on the idea that it was merely a composition statute designed to benefit creditors.[14] A municipal bankruptcy petition could not be filed until there was a plan of adjustment that a majority of the creditors had already approved. The judge could not confirm this plan until a supermajority approved it. Even then the bankruptcy judge could not confirm the plan unless it was, among other things, "in the best interests of the creditors."

This brings us to the first plausible interpretation of "best interests." One can argue that the most straightforward way of understanding "best interests" in a municipal bankruptcy is to give it the same meaning it had in

[13] See Eugene V. Rostow & Lloyd N. Cutler, Competing Systems of Corporate Reorganization: Chapters X and XI of the Bankruptcy Act, 48 Yale L.J. 1334, 1353 (1939).

[14] See, e.g., United States v. Bekins, 304 U.S. 27 (1938) (observing, among other things, that "the bankruptcy power may be exerted to give effect to a plan for the composition of the debts of an insolvent debtor, we find no merit in appellant's objections under the Fifth Amendment").

the context of a composition of a small business. "Best interests" is sensibly understood as establishing the idea that, as in the case of compositions involving small businesses, the rights of dissenting creditors of municipalities are to be assessed by whether it gives each of them at least as much as she would have received if left to her own devices outside of bankruptcy.

Given that the first municipal bankruptcy statutes styled themselves as composition laws, the argument goes, it makes sense to interpret the best-interests language in the same fashion as with ordinary compositions. It might seem odd to equate the financial affairs of a distressed municipality with those of a small dry goods merchant, but the prototypical municipal bankruptcy in the 1930s was not a city or a school system, but something much smaller and much simpler.

States regularly created instrumentalities to serve narrow and specialized purposes. A common example was an irrigation district. Such a district would borrow money and use it to pay for the construction of an irrigation system. Once completed, it supplied badly needed water to agricultural land. If all went according to plan, the irrigation system would increase the value of the land by more than the cost of the improvements. By virtue of the increase, the owners of the land would be able to afford new taxes that would, in turn, be enough to repay the debt.

The Great Depression destroyed the assumptions that brought these districts into being. Among other things, there was a collapse in commodity prices. The value of agricultural land plummeted. In many instances, the total value of the land in an irrigation district was less than the amount of the tax liens on it.[15] The owners of the land were better off walking away from the land rather than paying the taxes. No one had an incentive to work land subject to such a tax burden.

For their part, municipal creditors had no way of foreclosing on the land and exploiting its value for themselves. Creditors of a municipality lack most of the legal remedies that creditors of private debtors enjoy. They

[15] See, e.g., Ashton v. Cameron County Water Improvement District No. 1, 298 U.S. 513 (1936) (average market value of lands in the district did not exceed $75 per acre; total bonded debt per acre, principal and interest, was approximately $100).

cannot seize privately owned land. Their debtor was the irrigation district, not the landowners. The irrigation district itself had few assets. Even with respect to these assets (such as pieces of pipe used in the irrigation system), creditors typically are not able to reach them.

As a matter of state law, the assets of a municipality (the town hall or the fire trucks in the case of a city; pipes in the case of an irrigation district) are treated by the law as not being owned by the municipality, but rather as being held by it in "public trust" and therefore unavailable to the creditors. Municipal creditors could look only to the tax revenues that the municipality collected and, with respect to many irrigation districts, it collected none.[16]

When landowners in the irrigation district did not pay taxes, there was little that creditors could do. The legal rights of the creditors were limited to bringing a mandamus action against the tax collector and ordering her to raise the taxes necessary to pay the debt. In the 1930s, this remedy was largely toothless. Officials would resign from office in order to evade the writ of mandamus. People would run for tax collector on a platform in which they promised to go to jail rather than collect taxes.[17] As Justice Frankfurter famously observed, "the right to enforce claims against the city through mandamus is the empty right to litigate."[18] As he put it, "An unsecured municipal security is therefore merely a draft on the good faith of a municipality in exercising its taxing power."[19]

Given their modest rights under state law, creditors of a municipality were even more helpless than the distant suppliers of a distressed dry goods merchant. Here too a Coasean bargain between the bondholders and the municipality was desirable. If the creditors could agree to reduce the amount of the debt, the landowners would have an incentive to work the land and pay taxes on it.

[16] See Michael W. McConnell & Randall C. Picker, When Cities Go Broke: A Conceptual Introduction to Municipal Bankruptcy, 60 U. Chi. L. Rev. 425 (1993).

[17] See Faitoute Iron & Steel Co. v. City of Asbury Park, 316 U.S. 502, 511 (1942).

[18] See 316 U.S. at 510.

[19] 316 U.S. at 509.

Bondholders of the irrigation district stood to gain relative to what they would receive outside of bankruptcy if such a deal could be struck. As with creditors of small merchants who failed, however, the bankruptcy judge needs to ensure that, even when a majority of the creditors support the composition, it is in fact Pareto superior, that each dissenting creditor is receiving at least as much as she would receive if left to her own devices. Only then, the argument goes, is the plan in the best interests of creditors.

This account of "best interests" is easy to reconcile with larger bankruptcy principles. As set out in cases such as *Butner v. United States*[20] and reaffirmed in many cases since, bankruptcy takes nonbankruptcy rights as given. Creditors do not lose rights merely by happenstance of bankruptcy. These rights should be altered only if a particular bankruptcy policy requires it. Interpreting "best interests" to ensure dissenting creditors enjoy at least as much as they would receive outside of bankruptcy vindicates this idea. Municipal bankruptcy, like the traditional composition, is a creditors' remedy. It should be used only if it makes the creditors better off. The judge is a protector of substantive, nonbankruptcy rights.

This interpretation of "best interests," however, did not become clearly established in the 1930s nor in the decades afterwards. In contrast to the bankruptcy provision governing small businesses, the "best interest" language in the context of municipal bankruptcy was joined with the requirement that the plan be "fair" and "equitable." Each individual creditor had the right to insist that the plan was "fair, equitable, and for the best interests of the creditors."

The words "fair" and "equitable" were also terms of art with a long history, in this case a history that stretched back to the equity receiverships involving large railroads in the nineteenth century. In 1939, the Supreme Court found that the words "fair and equitable," in the context of corporate reorganizations, mandated absolute priority.[21] Senior creditors had a right to insist on being paid in full before junior creditors received anything.

Absolute priority cannot be mechanically transplanted to municipal insolvency. A corporate reorganization sorts out the rights of investors to a firm. The revenue stream that the firm produces in the future is divided

[20] 440 U.S. 48 (1979).

[21] Case v. Los Angeles Lumber Products Co., 308 U.S. 106 (1939).

solely among these investors. No one else is entitled to it. By contrast, a municipality produces a tax revenue stream, and a municipal restructuring must settle in the first instance how much of this revenue stream will go to satisfying the claims of investors and how much will be used to provide services to the taxpayers.

There were not many appellate opinions interpreting what "fair and equitable" meant in the context of municipal bankruptcy. At the very least, it required the judge to examine the taxing power of the municipality and spell out the justifications for the treatment of each class of creditor.[22] To be able to restructure the debt at all, the debtor had to make a "sufficient showing that the tax power was inadequate to raise the taxes to pay [the creditors]."[23] One can argue that in order to be "fair and equitable" the plan had to maximize the total revenue available to creditors. Alternatively, one could argue that creditors were entitled only to the tax revenue that is left after tax revenue is used to provide essential services.

The presence of the "fair and equitable" test, however, relieved courts from the need to focus on the "best interests of the creditors" language. However much "fair and equitable" provided for creditors, it was plainly more than the "empty right to litigate" that they had if they asserted their nonbankruptcy rights. When they did invoke the "best interests" language, it was often in the same breath as "fair and equitable." Over time the idea of "best interests of the creditors" became largely subsumed within the requirement that the plan be "fair" and "equitable." Courts never focused on what "best interests" meant.

In recent decades, creditors have devised increasingly stronger ways of collecting what they are owed outside of bankruptcy. No longer do they possess merely an empty right to litigate. As a result, the relationship between "fair and equitable" and "best interests" that was at the heart of how municipal bankruptcy was understood has been altogether changed. CPS illustrates.

Even though few think that CPS will be able to meet all of its obligations, some of CPS's bondholders are confident they will continue to be

[22] See Kelley v. Everglades Drainage District, 319 U.S. 415 (1943).

[23] Fano v. Newport Heights Irrigation District, 113 F.2d 563 (9th Cir. 1940).

paid. They hold what are known as alternative revenue bonds. These give their holders the ability to look to multiple different sources for repayment. Interest and principal on these bonds is to be paid in the first instance out of revenues that CPS receives from the state. If these prove inadequate, the bondholders are entitled to property tax revenues. If these are not enough and there is a default, property taxes increase automatically and the new taxes are turned over directly to the bondholders.

To put the matter concretely, if there were a default this year on CPS bond debt, the tax bill for someone who owned a $250,000 house in Chicago would rise automatically by more than $700. Moreover, in the event of default, Cook County must pay the bondholders directly. CPS will not be able to prevent the bondholders from being paid because, once there is a default, CPS never receives the tax revenue.

At the time the bonds were issued, CPS voted for the necessary tax increase and then immediately voted to abate the new tax. The abatement terminates automatically in the event of a default. In other words, the much larger taxes needed to pay the bondholders have already been put in place. Property owners so far have not needed to pay it, and some do not even know about it, but it is there nevertheless.

Ordinarily, municipal debtors, like other debtors, can use the money they have on hand to continue to operate instead of paying creditors. They can keep spending money until their creditors to vindicate their rights in court. Not so with the CPS. Even if CPS forced to shut down completely, the holders of alternative revenue bonds will still be paid outside of bankruptcy. If best interests requires the nonbankruptcy baseline, then individual alternative revenue bondholders would be able to demand more by asserts the best interests test than their class could demand by invoking the "fair and equitable" test. Indeed, being able to demand this much might make it hard to use Chapter 9 to restructure debt.

Even when creditors of corporations enjoy substantial nonbankruptcy rights, they must be careful about killing the goose that lays the golden eggs. Unless the corporation remains a viable going concern, they will not be paid. Such is not the case with holders of CPS alternative revenue bonds. Even if the school system collapsed completely, these bondholders would be able to tap Cook County's property tax revenues. One of the forces that generates the problems of the CPS—that lack of a tight connection between those who pay the taxes and those who send their children to the public schools—makes it possible for the creditors to be relatively indifferent to the future of public schools in Chicago. If Chapter 9 is structured to prevent creditors from acting in this fashion, then it may not make sense to import the small-business understanding of best interests into municipal bankruptcy law.

The justification for using the nonbankruptcy baseline as the measure of "best interests" arguably rests not on the *Butner* principle, but rather on its once having been a sensible way to assess whether a majority of creditors should be able to bind the minority. Using the nonbankruptcy baseline is only one way of interpreting best interests to protect dissenters, and it may no longer be an appropriate one given that the nonbankruptcy baseline has changed so dramatically. An alternative interpretation of "best interests" focuses on the protection of minorities directly. This is the focus of the next Part.

II. Best Interests and the Protection of Dissenters

When municipal bankruptcy laws were rewritten in 1976, its drafters believed that any plan that was "fair and equitable" was necessarily in the best interests of the creditors. The industrial strength remedies of the holders of CPS bonds had yet to be devised. The best-interests test was seen as toothless, and it was dropped. It was enough that individual creditors had the right to insist that the plan was "fair and equitable." Two years later, Congress rewrote and codified all of bankruptcy law, including the 1976 municipal bankruptcy statute. At this point, the "best-interests" test reappeared. One might be able to explain why it did by looking at the structure of the 1978 Bankruptcy Code.

When Congress overhauled the entire Bankruptcy Code in 1978, it made a major change in the "fair and equitable" test as it applied to Chapter 11 corporate reorganizations. No longer was it a right that an individual creditor could invoke. It was a right that only the creditors as a group could assert. In addition, the drafters gave creditors as a class the right to object to a plan that "discriminate[d] unfairly." Just as "fair and equitable" ensured that absolute priority is respected between senior and junior creditors, a prohibition on "unfair discrimination," another phrase that appeared in previous bankruptcy legislation, ensured equal treatment for creditors at the same priority level.

The “best interest” language was not included in Chapter 11 in the 1978 codification, but a provision was added that explicitly gave each individual creditor the right to insist, even when other creditors in its class consented to a plan of reorganization, that the plan provide her with at least as much as she would have received in a Chapter 7 liquidation.[24] Those who drafted this language (and bankruptcy lawyers ever since) have called this the “best interests” test. This provision does not use the nonbankruptcy baseline, but by referring to liquidation value it too is protecting dissenters with a substantive entitlement.

Once Chapter 11 took this shape, those who were codifying bankruptcy law had to confront the question of what to do with the municipal bankruptcy law that had been rewritten only two years before. No one pushed for major changes, but the law still needed to be brought into the framework of the new Bankruptcy Code. Under the 1976 iteration of municipal insolvency, as with previous corporate reorganization statutes, every creditor could insist upon a plan that was “fair and equitable.”

The drafters of the 1978 Bankruptcy Code brought the basic structural changes found in Chapter 11 to Chapter 9. As they had with Chapter 11, they decided that in Chapter 9 only a class of creditors could invoke the “fair and equitable” test. Once they allowed a majority in a class to bind the minority, they needed to decide what sort of protection dissenting creditors within each class should enjoy.

As just noted, Chapter 11 guaranteed the dissenters the same amount as they would realize in Chapter 7, but there was nothing analogous to a liquidation in the context of a municipality. Some other protection therefore needed to be given to dissenters. Instead of providing a hard-edged substantive benchmark, the drafters reintroduced the open-ended “best interests” language that had been dropped only two years before.

It is possible to make a link between “best interests” and nonbankruptcy rights, but it was no longer as obvious a link in the 1970s as it had been in the 1930s. By this time, it was manifest that the finances of a large city were nothing like those of an irrigation district. The analogy between a

[24] 11 U.S.C. §1129(a)(7).

municipality and a small business was no longer so compelling. Restructuring the debt of a large school district bears little resemblance to the composition of the debt of a dry-goods merchant.

Notwithstanding its inability to pay its creditors on time, a city like New York would never be able to take advantage of a municipal bankruptcy regime that was built around the premise that it was merely a composition. Bondholders of a large municipality were too diverse and the financial affairs of a large city too complex for it to be even remotely possible for a majority of all the creditors to coalesce around a plan before the case was even begun.

One can argue that, from Congress's perspective in 1978, the phrase "best interests" was not in the first instance protecting nonbankruptcy rights per se, but rather protecting a dissenting minority in a class when a supermajority agreed to a restructuring of their debt. Chapter 9, like Chapter 11, encourages parties to reach a bargain that avoids a costly judicial hearing. The prospect of such a hearing in which the judge assesses whether a plan is "fair and equitable" provides the background against which the debtor negotiates with each class of creditors. The ability to bargain in the shadow of an expensive judicial process is valuable, but it comes with risks. The "best interests" test is what protects a dissenting minority if for some reason there is something suspect about the bargain the class strikes with the debtor.

The best-interests test, under this view, is not about ensuring that each creditor receives as much as she would have received outside of bankruptcy. The outer limit of the creditors' substantive entitlement is set by the "fair and equitable" rule, not by what they might have received outside of bankruptcy. Even if the creditors as a class would be able to divert the entire tax revenue stream outside of bankruptcy, they may lack the ability to do it inside. The most they can insist upon is that the plan is fair and equitable, and this may not entitle them to so much that it would deprive the municipality of the ability to provide essential services.

The Bankruptcy Code has a number of provisions that do much to ensure that, if a supermajority of those holding claims in a class favors a particular course of action, it is likely a course of action that makes sense for each member of the group. Claims can be put in the same class only when they are substantially similar.[25] In addition, each claim in a class must receive the same treatment.[26] Moreover, the bankruptcy judge is empowered to designate—that is, disqualify—the vote of a creditor who votes in good faith.[27]

Putting similar claims in the same class, treating each identically, and ensuring that votes are cast is good faith may not be enough, however. Even if claims have the same legal attributes and are treated the same way, the holders of such claims may have different relationships with the debtor. In the bankruptcy of the City of Stockton, for example, the class of general creditors included not only the claims of bondholders, but also health benefit claims of retired workers. The retirees held pension claims against the City as well. They might support a plan that gave short shrift to their health benefits if it provided for sufficiently favorable treatment for their pension benefits.

It might seem that a judge should not allow health-benefit claims to be classified with those of bondholders, but there is a well-developed classification jurisprudence in Chapter 11 cases that establishes that claims with the same legal attributes can be put in the same class.[28] One can argue that Chapter 9 should have different classification rules, but Chapter 9 incorporates Chapter 11's classification rules by reference and nothing requires that these rules be interpreted differently.

One can also argue that a judge should designate votes when a creditor holds multiple claims and casts a vote in one class in order to promote its stake in another class. But again Chapter 11 caselaw is otherwise. Creditors who hold claims in multiple classes are entitled to vote each of their claims in a way that maximizes the value of all their claims against the debtor.[29]

But even if these rules were interpreted differently in Chapter 9, there are always going to be ways in which some creditors in a class will not have

[25] 11 U.S.C. §1122.

[26] 11 U.S.C. §1123(a)(4).

[27] See 11 U.S.C. §1126(e).

[28] See, e.g., In re Woodbrook Associates, 19 F.3d 312 (7th Cir. 1994) (forcing separate classification because the legal rights are not identical).

[29] See, e.g., Figter Ltd. v. Teachers Insurance & Annuity Association, 118 F.3d 365 (9th Cir. 1997).

the same set of interests. Those who oppose the plan may not simply be hold-outs trying to throw sand in the gears of the restructuring in order to gain more favorable treatment for themselves. It is therefore useful to have a separate check on whether, in any particular case, it makes sense for the majority of claimholders in a particular class to bind the minority. One can easily understand the "best interests" test as serving this function.

Congress could have made a specific reference to nonbankruptcy entitlements instead of (or in addition to) the "best interests" language. Indeed, Congress did this in 2016 when it drafted the insolvency legislation governing Puerto Rico and its instrumentalities.[30] But, standing on its own, the "best interests" test does not require that the court use such a substantive benchmark.

An alternative way to protect dissenters (and hence a sensible way to interpret the best-interests test) is to look to process. To find that the dissenter can be bound to the class-wide vote, the judge looks at the competing interests of the majority of the creditors and the dissenters and asks whether binding the dissenters is reasonable under the circumstances. The judge takes a look at the bargain that the group has struck with the debtor and how it was reached. If it is a sensible deal that a reasonable creditor would take, then dissenters are going to be bound to it, but not otherwise.

The more the majority shares common ground with the dissenting creditor, the more confident one can be that the dissenting creditor is

[30] The Puerto Rico Oversight, Management, and Economic Stability Act ("PROMESA") in §314(b)(6) provides the court can confirm a plan only if the plan is "in the best interests of creditors, which shall require the court to consider whether available remedies under the nonbankruptcy laws and constitution of the territory would result in a greater recovery for the creditors than is provided by such plan." PROMESA stops short of equating its best interests test with the nonbankruptcy baseline. The judge must only "consider" the nonbankruptcy remedies. But it does not seem useful to use this language from 2016 to interpret the language in Chapter 9 that Congress enacted in 1978. Among other things, this language reflected considerable lobbying between competing groups of Puerto Rican bondholders.

engaging in hold-up behavior. The more the other creditors have mixed motives, even if they are not so conflicting that they require a separate classification or a designation of their vote, the more the judge needs to focus on the substantive question of whether the plan is a sensible accommodation of the rights of the creditors and the needs of the municipality.

Under this interpretation of the language, "best interests" is what protects the dissenting minority when the majority has agreed to take a plan and has given up its right to a hearing in which the judge assesses whether the plan is fair and equitable and does not discriminate unfairly. Seen from this perspective, the best-interest test requires the judge to ask whether it makes sense to bind the dissenters by the majority's decision to waive their right to insist on such a hearing. The court should ask whether, in light of all the circumstances, the plan is one that a rational creditor, not intent on hold-up behavior, would accept.

Chapter 9 creates a bargaining environment that allows creditors as a group to negotiate with the debtor and avoid a time-consuming and expensive judicial procedure. To be effective, the rules need to overcome the holdout problem and, at the same time, ensure that the rights of the minority are being respected. Under this interpretation, the "best interests" test is serving this second function.

This process-based approach to protecting the interests of the dissenting creditor focuses directly on the matter at hand. One can argue that it makes sense of the structure of Chapter 9 and the distinction it draws between class-based and individual-based rights. By focusing on process, this interpretation makes the "fair and equitable" principle and the prohibition on "unfair discrimination" the focal point for ensuring that the substantive rights of the creditors in any particular class are protected.

This understanding of best interests leaves the bondholders of CPS in a much weaker position than they would be in if they could use "best interests" as a way to demand as much as they would have received outside of bankruptcy. But it might play an important role nevertheless. One of the major players in a CPS bankruptcy is likely to be J.P. Morgan. It has major provider of short-term funds to CPS. At the same time, it also is a major creditor of the City of Chicago and has many dealings with it.

J.P. Morgan might agree to a restructuring of its CPS debt on much less favorable terms than other similarly situated creditors (and much less than the creditors were entitled to under the “fair and equitable” test) in order to protect its relationship with the City of Chicago. Creditors who find themselves outvoted might be able to force the judge to take a hard look at the plan if this interpretation of “best interests” were adopted. This is an enterprise altogether different from asking what these creditors would have received outside of bankruptcy, but it has consequences nevertheless.

An interpretation of the best-interests that focuses on protecting a dissenting creditor in a class, however, does not fit the language of the statute perfectly. The statute does not require the judge to ask whether the plan is in the interest of the particular creditor who dissents, but rather whether it is in “the best interests of *creditors*.” To be sure, what is in the interests of the class of creditors may also in the interests of each member of the class. But the section does not speak to the rights of the dissenting creditor who lodges an objection or even to particular classes of creditors, but rather to creditors generally. This introduces another possible interpretation, one that looks at creditors across classes.

The best-interests test may direct the bankruptcy judge, after satisfying herself that all the discrete protections of Chapter 9 have been met, to make a final assessment of how the plan affects the creditors collectively. In a simple case in which creditors have the same legal rights and occupy the same class, there may be little practical difference between this approach and one that focuses on process, but municipal creditors today come in many different forms and have many different rights outside of bankruptcy. Restructuring the debt of a municipality also requires making peace with other constituencies—not least the state legislature and city workers. Making a general assessment of how, once the dust settles, the plan treats all the creditors collectively is different from asking how a plan treats a dissenting creditor within a particular class.

III. Best Interests as a Reality Check

An alternative way of understanding the best-interests test starts by connecting it to other statutory directives, in particular Chapter 9’s requirement that the plan be "feasible."[31] In Chapter 11, the bankruptcy judge is not supposed to confirm a plan if it will simply lead to another reorganization.[32] When a firm has no value as a going concern and its assets are worth more deployed elsewhere, liquidation is the sensible course of action. There is no virtue in keeping a restaurant open if no one wants to eat there. In Chapter 9, the court must also ensure that the plan is "feasible," that again the debtor can meet its obligations under the plan, but there is no parallel to liquidation in Chapter 9.

CPS or some other entity must continue to provide public education to the children of Chicago. The need to ensure that resources are available to provide this service makes a school system altogether different from a Chapter 11 of a restaurant that serves bad food. The inability to liquidate a municipality and cease providing the relevant services requires that "fair and equitable" be interpreted differently in Chapter 9 than in Chapter 11. This in turn affects how one might interpret "best interests."

One can argue that the various requirements of Chapter 9 should be interpreted in a way that provides a municipality with at least one path to restructuring its debts and still provide essential services.[33] Seen from this perspective, the idea of feasibility is tightly connected to what is "fair and equitable," what does not "discriminate unfairly," and what is in "the best interests of creditors."

[31] 11 U.S.C. §942(b)(7).

[32] See 11 U.S.C. §1129(a)(11). This provision is commonly called the "feasibility" test, even though, as with Chapter 11's "best interest" test in §1129(a)(7), this language not actually appear there.

[33] What counts as an essential service is, of course, contestable. It cannot be whatever the municipality is providing. Nor does it prevent some municipalities and the services they provide from disappearing completely. Given the broad definition of "municipality" in Chapter 9, not every municipality provides an essential service or is worth keeping. New York's off-track betting corporation was a "municipality" within the meaning of Chapter 9, but there were no services it provided so essential that they compete with the creditors' right to payment. See In re New York City Off–Track Betting Corporation, 427 Bankr. 256 (Bankr. S.D.N.Y. 2010).

This idea can also be located in the history of municipal bankruptcy. In the first municipal insolvency statutes, there was no separate requirement that the plan be feasible. The idea of feasibility was built into the way "fair and equitable" was understood in the context of a municipal insolvency.[34] In the view of the courts that confronted the question, the "fair and equitable" test reflected some judgment about how much the tax base of the municipality should be available to pay the creditors given that it must continue to serve to those who live there. To be confirmable, a plan had to allow the municipality to keep enough revenue to provide essential services. Only what was left would go to the creditors. The "fair and equitable" principle did not give creditors an unlimited right to the tax revenue that the municipality produced. Instead, it requires the judge to assess whether the amount being offered under the plan "is all the [municipality] is able to pay under the circumstances."[35]

This approach does not necessarily ensure the survival of a particular entity, nor does it require that the entity in Chapter 9 continue to provide the relevant services. A school system might liquidate and another might replace it. A municipality might cease providing police and fire protection and turn to some other entity, such as the county or neighboring municipality to provide it. The idea is only that the debt needs to be reduced enough so that it is possible to generate sufficient tax revenue to pay for the essential service.

Under this view, feasibility and "fair and equitable" work as complements. Allowing the municipality to keep the revenue needed to provide essential services makes the plan "feasible," while turning over the balance is what makes it "fair and equitable." One can argue that the "best interests" test needs to be assessed against this backdrop.

[34] See In re Mount Carbon Metropolitan District, 242 Bankr. 18, 33 (Bankr. Colo. 1999). This is, in any event, how, according to the legislative history, Congress understood the "feasibility" requirement when it introduced it into Chapter IX in 1976. See H.R. Rep. 94-686, H.R. Rep. No. 686, 94th Cong., 2d Sess. 1976, 1976 U.S.C.C.A.N. 539, 1975 WL 12383.

[35] Lorber v. Vista Irrigation District, 127 F.2d 628 (9th Cir. 1942).

When a complicated bargain involving many classes of creditors is struck, the judge must apply the "fair and equitable" test for each class that does not consent to the plan. But she should also make an assessment of the recovery the creditor body as a whole is receiving. Under this view, the best-interests test looks not at the relationship between a creditor and the class to which she belongs, but rather to the creditor body as a whole and how the plan treats them collectively. The question is not so much how any particular creditor is being treated, but rather whether the creditors as a group are getting as much as they can reasonably expect under the circumstances.

The best-interests test provides a last look at a plan after all the other dictates of Chapter 9 have been satisfied. Under this view, the best-interests test does not implicate the substantive rights of individual creditors. Bankruptcy law protects the individual creditor in the first instance through the ability of her class to negotiate on her behalf and, if negotiations fail, insist on a judicial hearing in which it can argue that the plan is not "fair and equitable" or that it "discriminates unfairly." The individual rights of dissenting creditors are protected from advantage-taking by the majority not through the best-interest test, but through the requirements that only similar claims be grouped together, that they be treated the same, and that votes cast in bad faith be designated.

This approach to Chapter 9 is consistent with the roots of "fair and equitable" and "best interests," and it accommodates Chapter 9 to the radically different forms of debt that municipalities have today. The financially distressed municipal debtor in Chapter 9 is no longer an irrigation district that has made a single bond issue, but rather a city or school district with massive pension and other unfunded retiree obligations. It has issued bonds, tax anticipation notes, certificates of participation, and many other exotic financial instruments. Striking a deal that gains sufficient consensus among all the players is a long and difficult process, and it may make sense to see the "best interests" test as requiring the judge at the end of the day to take a synoptic look at how the plan treats the creditors as a group.

Financially distressed municipalities today often carry substantial unfunded pension and retiree obligations. These obligations often represent the lion's share of its indebtedness. Retirees do not hold diversified portfolios. Indeed, its retirees are not entitled to social security payments and may have no other source of income. Moreover, many, like CPS, depend upon a unionized workforce, and there may be only a limited ability to reduce retirement benefits and still ensure either that the teachers continue to work or that replacements for them are found.

There will be strong political pressure to craft plans that subject institutional bondholders to significantly worse treatment than the retirees. At the same time, the state might offer additional aid that is itself steered to some creditors, but not others. The judge must decide whether she can confirm a plan that treats creditors with the same legal rights differently from others. To decide whether such a plan passes muster when a class of creditors opposes it, the judge must decide whether it "discriminates unfairly." If a class approves such a plan, but individual members of the class dissent, the court must ask whether the plan is in the "best interests of the creditors."

The idea of "unfair discrimination," as developed in the late 1930s and early 1940s, focused on protecting outside investors from insiders who had an incentive to employ various devices to channel assets to themselves.[36] But, like "best interests," the term "unfair discrimination" is open-ended. The bankruptcy judge in Detroit's bankruptcy found that the prohibition against "unfair discrimination" still tolerated substantial differences in the way that various classes of creditors were treated. The court observed that, in the context of Chapter 9, "fairness is a matter of relying upon the judgment of conscience. That is all the Congress intended in so broadly articulating the unfair discrimination test. . . ."[37]

The bankruptcy judge in Detroit actively pushed the parties towards a plan that most creditor constituencies accepted, though some acquiesced only after considerable arm-twisting.[38] The court approved a plan in which

[36] For example, questions might arise when a bondholder received undisclosed payments from the debtor in another capacity, such as serving as its fiscal agent. See American United Mutual Life Insurance. Co. v. Avon Park, 311 U.S. 138 (1940).

[37] In re City of Detroit, 524 Bankr. 147 (Bank. E.D. Mich. 2014).

[38] For an excellent discussion of the activist role that the court played in the case, see Jacoby, note 8 supra.

retirees enjoyed favorable treatment relative to institutional investors. In its view, this favoritism advanced the city's interest in preserving its relationships with its employees. In addition, it was consistent with the way pension obligations were singled out for protection under the Michigan constitution, and the higher expectations of the pension holders. Perhaps most important, the more favorable treatment of the pension holders was part of the warp and woof of a Grand Bargain struck with many constituencies, including the state. This bargain brought $800 million additional dollars into the city's coffers.

The judge interpreted the best-interests test in the same spirit as he interpreted the prohibition on unfair discrimination. He found that it entitled the dissenting creditors only to an assessment on the part of the bankruptcy judge that they are receiving "all that they can reasonably expect under the circumstances."[39]

There is much to criticize in the Detroit bankruptcy, but in a world in which feasibility requires the existence of at least one feasible plan, the "fair and equitable" test and the antidiscrimination rule provides creditors with their primary substantive protections. Beyond these, it may make sense to interpret the best-interest test as requiring the judge to take stock and assess whether the plan makes sense for the creditor body as a whole, given the alternatives. This interpretation of "best interests" is not focused on the individual creditor and whether her ox is being gored. Instead, it requires the judge to ask how the creditors as a whole are doing, looking across classes of creditors.

CPS illustrates how this last interpretation of best interests might play itself out. The amount of aid that CPS receives from the state each year is politically contested. In particular, the state contributes to the pension funds of teachers outside of Chicago, but not inside. It is not at all implausible that state aid will come in the form of additional funds for pensions that is conditioned on the retirees receiving favorable treatment under the plan. It will not be willing to extend pension aid, if it allows for greater cutbacks in pensions and makes more money available for bondholders.

[39] 524 Bankr. at 219.

A settlement with the teachers will likely involve not only restructuring their pensions, but also the level of contributions CPS makes to their pension fund going forward. Like other state workers, Chicago teachers must contribute 9% of their salaries to their pensions. A number of years ago, however, CPS agreed to pick up most of this contribution.[40] This obligation costs $160 million a year. CPS at the moment is contractually obliged to make these payments through 2020. A deal might involve reducing this obligation after 2020. It lightens the burdens of CPS, but is not technically a restructuring of indebtedness.

Similarly, reductions in the number of teachers and increases in average class size do not directly translate into reduced indebtedness, but may be a part of any grand bargain that sorts out the problems of the Chicago public schools and puts it on a sustainable path. The bargain will likely include a number of school closings. Such changes will weigh in the balance of sacrifices that teachers make even if they do not formally count as a reduction in the amount they are owed.

In putting together a grand bargain, there will be winners and losers among the creditors. This is inevitable. Under this interpretation of the "best interests" test, a dissenting creditor in a class cannot complain about whether the vote of the majority of their class should be able to bind her or even what she is receiving under the plan. Instead, she can insist only that, quite apart from her own treatment under the plan, the grand bargain itself gives creditors across all classes as much as they can reasonably expect.

This interpretation of "best interests" centers around the idea that a plan that restructures the debt of a large municipality will have to be a grand bargain that brings together multiple, diverse constituencies. To gain sufficient consensus, the judge sometimes must be heavy-handed. When there is arm-twisting and jaw-boning, it is useful to have the judge take several steps back at the end and assess the bargain as a whole.

Such an interpretation of "best interests" co-exists with an expansive view of what the judge is supposed to do in Chapter 9. This approach fits agreeably with what we have seen in recent municipal bankruptcies, such as that of the City of Detroit and the City Stockton. In Stockton, for

[40] The pick-up does not apply, however, to teachers who started after January 1, 2017.

example, the unsecured creditors came with different interests and different agendas. The bankruptcy judge "looked long and hard at the history of this case and the responses that have been made and considered the alternatives, including the alternative of putting the whole situation back to square one," and concluded that the parties would be "running up many more millions of dollars in terms of expense for the City for what I view as probably not likely very much difference, and that's because this plan, I'm persuaded, is about the best that can be done."[41]

IV. Conclusion

The three interpretations of "best interests" offered here reflect different visions of the bankruptcy judge. In the end, even a conception of "best interests" that looks collectively at the creditors as a group is as grounded in the text, history, and purpose of the statute as any other. What distinguishes it is the role that it envisages for the bankruptcy judge. Instead of protecting nonbankruptcy rights or ensuring that the process is fair to dissenting members of a class, the bankruptcy judge who uses "best interests" to assess the overall fairness of the bargain struck with the many constituencies is likely to be someone who immerses herself deeply in bringing the parties together and crafting the ultimate plan.

Further complicating the question of how the Bankruptcy Code should be interpreted is the peculiar status of bankruptcy judges. One could imagine a world in which bankruptcy judges were housed in an administrative agency that enjoyed rule-making power under the Bankruptcy Code. In such a world, the administrative agency might engage in formal rule-making that interpreted the "best interest" language, and it would be entitled to deference under *Chevron*.[42] The administrative agency could decide the most sensible way to resolve this statutory ambiguity.

But, even if housed in an administrative agency, the bankruptcy judges themselves would not be able to resolve the ambiguity and enjoy any degree of deference. Bankruptcy judges are dispersed. There is no mechanism for ensuring uniformity. They have no ability to fashion an interpretation

[41] Franklin High Yield Tax-Free Income Fund v. City of Stockton, 542 Bankr. 261 (9th Cir. B.A.P. 2015).

[42] See Chevron, Inc. v. Nat. Res. Def. Council, Inc., 467 U.S. 837 (1984).

entitled to be treated as having the force of law analogous to rule-making that has gone through a notice-and-rulemaking process.[43] At best, if bankruptcy judges were housed in an administrative agency, their opinions would be entitled only to relatively weak *Skidmore* deference and reviewing their decisions, their opinions would represent at best a "body of experience and informed judgment to which courts and litigants may properly resort for guidance."[44]

But bankruptcy judges are not housed in administrative agencies in any event. They are adjuncts of the district court and appointed by the court of appeals. They lack the political accountability to which, in theory at least, administrative agencies are subject. More to the point, the Supreme Court has consistently unwilling to give them deference across any dimension.[45] As recently as last year, the Court reversed a bankruptcy judge who exercised his discretion to approve a disposition of a case that was Pareto superior. The Court found it was beyond a bankruptcy judge's power to bless a distribution of assets that left some better off and left no one worse off.[46] Yet it is exactly this sort of liberty that a bankruptcy judge in a case is exercising when "unfair discrimination" is interpreted broadly and "best interests" focuses on creditors collectively.

Arguing that the bankruptcy judge should have freer rein in Chapter 9 than elsewhere is hard. Indeed, on the face of it, the bankruptcy judge has much more limited powers in Chapter 9. Section 904 expressly prohibits the court from interfering with any political or governmental power of the debtor or interfering with any property or revenues of the debtor, or with the debtor's use or enjoyment. There is no bankruptcy estate over which the judge has control as there is in Chapter 7 and Chapter 11.

The most powerful argument in favor of a broad conception of best interests may rest on the idea that alternative interpretations do not provide financially distressed municipalities such as CPS with a way to restructure their debt. In Illinois, for example, it may not be possible to

[43] See United States v. Mead Corp., 533 U.S. 218 (2001).

[44] See Skidmore v. Swift & Co., 323 U.S. 134, 140 (1944).

[45] See Douglas G. Baird & Anthony J. Casey, Bankruptcy Step Zero, 2012 Sup. Court Rev. 203 (2013).

[46] See Czyzewski v. Jevic Holding Corp., 580 U.S. • • • (2017).

restructure any of its pension obligations outside of bankruptcy. The Illinois Supreme Court has found these sacrosanct under the state constitution, and it does not seem that they can be taken away from individual workers or retirees without their individual consent.[47]

But it is not obvious that Chapter 9 should be the last safety net. Making it a safety net removes the pressure from others (in particular the state itself) to solve the problem. The responsibility to provide essential services ultimately rests with the state. Municipalities are all, in one way or another, its creatures.

[47] Heaton v. Quinn (In re Pension Reform Litigation), 32 N.E.3d 1 (Il. 2015).