RELIEVING INSOLVENT MUNICIPALITIES: NEW YORK'S EMERGENCY MORATORIUM ACT AND FEDERAL BANKRUPTCY LAW

New York City, one of several metropolitan areas threatened with fiscal insolvency,[1] faced possible bankruptcy in 1975. In response to the city's financial difficulties the New York legislature passed the Emergency Moratorium Act (EMA) for the City of New York.[2] In *Ropico v. City of New York*,[3] holders of New York City notes contended that the EMA conflicted with the federal Bankruptcy Act's[4]

1. In 1976 the average revenue per capita from local sources was $426 per resident while the average per resident debt was $1,052 for cities of over one million in population. U.S. NEWS & WORLD REPORT, April 5, 1976, at 51 (Bureau of the Census statistics). *See generally City Expenses Outstrip Income 2.7%*, AM. CITY & COUNTY, Dec., 1976, at 86.

2. 1975 N.Y. Laws (Extraordinary Session), ch. 874, *as amended by* ch. 875 (Consol. 1976).

Section 3 of the Act provides that

> . . . During the moratorium period, and notwithstanding any inconsistent provisions of any law, general, special, or local, or of any agreement or short-term obligation, no act shall be done, and no action or special proceeding shall be commenced or continued in any court in any jurisdiction, seeking to apply or enforce against the city, or any political subdivision, agency, instrumentality or officer thereof, or their funds, property, receivables or revenues, any order, judgment, lien, set-off or counterclaim on account of any short-term obligation, or the indebtedness or liability evidenced thereby, or seeking the assessment, levy or collection of taxes by or for the city or the application of any funds, property, receivables or revenues of the city on account of any such short-term obligation, or the indebtedness of liability evidenced thereby, although the payment of such short-term obligations may be due by the terms thereof or any general or special local law or agreement.

Id.

Section 4 provides that

> During the moratoruim period, and notwithstanding any inconsistent provisions of any law, general, special or local, or of any agreement or short-term obligation, no action or special proceeding shall be commenced or continued upon any short-term obligation, or any indebtedness or liability evidenced thereby, although the payment of such short-term obligation may be due by the terms thereof or any general or special local law or agreement.

Id.

3. 425 F. Supp. 970 (S.D.N.Y. 1976).

4. The Bankruptcy Act of 1898, §§ 1-755, 11 U.S.C. §§ 1-1255 (Supp. IV 1974). *See* notes 16-18 *infra*.

prohibition[5] against imposing compositions[6] on unwilling creditors. Rejecting this view, the *Ropico* court held that the EMA merely created a lawful extension of New York City's debt without violating the Bankruptcy Act composition provisions.[7]

The conflict in *Ropico* emerged following unsuccessful attempts by the New York legislature to solve New York City's fiscal crisis.[8] In 1975, after failing to rescue the city through loans, the legislature passed the EMA.[9] The Moratorium suspended, for a period of three years, all payments of principal on short-term notes which matured in 1975 and 1976.[10] Noteholders were given the option of exchanging their notes with at least eight percent interest due for longer-term obligations having an interest rate of at least six per cent. Notehold-

5. The proscription is contained in § 83(i), 11 U.S.C. § 403(i) (1970).

6. A composition has been described as "an arrangement between an insolvent and his creditors, whereby the creditors accept an amount equal to or less than the whole of their claims, for the sake of some payment at a future time." Ellison, *The Recent Revision of the Federal Municipal Bankruptcy Statute: A Potential Reprieve for Insolvent Cities?* 13 HARV. J. LEGIS. 549, 553 n.21 (1976). The term therefore refers to both plans which contemplate reductions in payment and those plans, called "extensions," that provide for payment in full at a later time. Under Chapter IX, a composition includes "provisions modifying or altering the rights of creditors generally, or of any class of them, secured or unsecured, either through issuance of new securities of any character, or otherwise." § 83(a), 11 U.S.C. § 403(a) (1970). This description apparently includes extensions.

However, other areas of the Bankruptcy Act draw a distinction between compositions and extensions. *See, e.g.*, Chapter XIII, § 606(7), 11 U.S.C. § 1006(7) (1970) (wage earners' plans); § 203, 11 U.S.C. § 603 (1970) (agricultural compositions and extensions).

7. 425 F. Supp. 970 (S.D.N.Y. 1976).

8. The legislature decided to take action after the city, unable to sell its securities on the market, faced default. In June 1975, the state advanced $800 million to the city. 425 F. Supp. at 973. Subsequently the legislature passed the New York State Municipal Assistance Corporation Act. N.Y. PUB. AUTH. LAW §§ 3001-3040 (McKinney Supp. 1977). This Act created the Municipal Assistance Corporation (MAC), a "corporate governmental agency and instrumentality of the state," authorized to raise money for the city by issuing its own bonds. MAC bondholders enjoyed priority over wage earners, welfare recipients, and other creditors in claiming revenues. 425 F. Supp. at 973.

9. In September 1975 the state legislature met in Extraordinary Session and passed the New York State Financial Emergency Act for the City of New York, including the EMA. 1975 N.Y. Laws (Extraordinary Session), Chapters 868-70 (Consol. 1976).

10. *See* note 2 *supra*. Additionally, the Emergency Financial Organization Act called for the establishment of an Emergency Financial Control Board to supervise the city's management and to institute a financial plan to restore the city financially within three years. *Id.* §§ 5-8. The Act also established a wage freeze for those city employees who had not already agreed to one. *Id.* § 10. Finally, the Act called for New York State to purchase $750 million in MAC bonds. 425 F. Supp. at 973.

ers who refused an exchange could receive six per cent interest, plus any amount held necessary under state or federal law, on their existing notes until the principal was repaid.[11]

Plaintiffs in *Ropico* contended that the EMA violated section 83(i) of the Bankruptcy Act.[12] Section 83(i) provides that, "no state law prescribing a method of composition of indebtedness shall be binding upon any creditor who does not consent to such composition, and no judgment shall be entered which would bind a creditor to such a composition without his consent."[13] The creditor-plaintiffs argued that the EMA constituted a state-imposed composition in conflict with the federal bankruptcy power and must be void as pre-empted by federal law.[14]

Chapter IX of the Bankruptcy Act of 1898 governs municipal bankruptcy law. This chapter,[15] known as the Municipal Bank-

11. MAC offered private noteholders an exchange of maturing notes for MAC bonds due July 1, 1986, at 8% interest. Noteholders who did not accept these conditions were foreclosed from instituting action on the bonds until the Act's expiration date, November 15, 1978. 425 F. Supp. at 975.

12. § 83(i), 11 U.S.C. § 403(i) (1970).

In addition to the Bankruptcy Act challenge, plaintiffs argued that the EMA imposed an impairment of contract in violation of the Contract Clause. U.S. CONST. art. I, § 10, cl. 1. The court upheld the act, finding a modification of the method of repayment rather than an impairment of credit. 425 F. Supp. at 976-77. Plaintiffs also alleged a deprivation of property without due process of law, a claim summarily rejected by the court on the basis of the state's overriding police power in time of emergency. *Id.* at 977. A third argument, that the EMA violated the Equal Protection Clause by denying short-term noteholders rights enjoyed by unaffected creditors, was rejected upon a finding of a rational basis for the classification. The court held that the urgency of repaying maturing short-term notes over other city obligations justified the classification. *Id.* at 977-78. Additionally the court rejected a challenge to the EMA under the full faith and credit clause. *Id.* at 978. *See* note 38 *infra* for discussion of full faith and credit challenges to the EMA.

13. 11 U.S.C. § 403(i) (1970).

14. 425 F. Supp. at 978-81. The Bankruptcy Act of 1898 is a legislative exercise of the federal bankruptcy power. The Constitution renders the federal government supreme power over bankruptcy. U.S. CONST. art. I, § 10. All provisions of Chapter IX are superior to state bankruptcy laws in conflict with that chapter. West Coast Life Ins. Co. v. Merced Irr. Dist., 114 F.2d 654 (9th Cir. 1940), *cert. denied*, 311 U.S. 717 (1941).

Where a state law conflicts with a federal law, the federal law is supreme and the state law is pre-empted. *See* Rice v. Santa Fe Elevator Corp., 331 U.S. 218 (1947); Hines v. Davidowitz, 312 U.S. 52 (1941). For studies on pre-emption, see Note, *Conceptual Refinement of the Doctrine of Federal Preemption*, 22 J. PUB. L. 391 (1973); Note, *Preemption Doctrine: Shifting Perspectives on Federalism and the Burger Court*, 75 COLUM. L. REV. 623 (1975).

15. Chapter IX of the Bankruptcy Act of 1898, §§ 81-84, 11 U.S.C. § 401-404, *as amended* by Pub. L. No. 94-260, 90 Stat. 317 (1976).

ruptcy Act, establishes procedures by which local taxing agencies may settle with creditors through composition. Due to the essential nature of the local agencies and the services they perform, the Bankruptcy Act denies agencies the option to cease operating.[16] Prior to 1975, Chapter II received little attention, since its provisions were applied almost exclusively to local service districts.[17]

Section 83(i) as originally enacted did not require creditor assent to any composition.[18] The section was designed to ensure that the Municipal Bankruptcy Act would not impermissibly interfere with traditional state control over municipalities.[19] The Supreme Court in *Faitoute Iron & Steel Co. v. City of Asbury Park*[20] held that the original section 83(i) did not affect state laws governing municipal insolvency. In *Faitoute*, the Court found a New Jersey Act requiring creditors to accept a later maturity date and lower interest rates to be consistent with the original section 83(i).[21] Congress, however, overruled *Faitoute* by enacting a proviso to section 83(i).[22] This proviso, prohibiting compositions without the consent of creditors, was designed to protect creditors' rights and to ensure uniformity of those

16. Sections 81-84, 11 U.S.C. §§ 401-404 (1970). Although a municipal corporation, unlike other corporations, may not go out of business, it may file a plan of composition in bankruptcy. Chapter IX prescribes the procedures and rules for such composition. The purpose of Chapter IX is to provide an insolvent municipality with a forum in which to meet with its creditors and develop a plan mutually beneficial to both debtor and creditor. H.R. REP. No. 207, 73d Cong., 1st Sess. (1933).

17. Congress enacted Chapter IX during the Depression after many small towns and service districts defaulted on their obligations. Most Chapter IX litigation has involved such service districts and small cities. Patterson, *Municipal Debt Adjustment Under the Bankruptcy Act*, 90 U. PA. L. REV. 520, 522 (1942).

18. The section read in its entirety: "Nothing contained in this chapter shall be construed to limit or impair the power of any State to control, by legislation or otherwise, any municipality or any political subdivision of or in such State in the exercise of its political or governmental powers, including expenditures therefor." Bankruptcy Act of 1898, § 83(i), 50 Stat. 659 (1937) (amended 1946, current version at 11 U.S.C. § 403(i) (1970)).

19. Section 83(i) was added to the Municipal Bankruptcy Act in 1937 after the original act was declared an unconstitutional infringement on state sovereignty. Ashton v. County Water Improvement Dist., 298 U.S. 513 (1936).

20. 316 U.S. 502 (1942).

21. The plan approved by the Court in *Faitoute* was accepted by only 85% of the city's creditors. The Court, however, found that the state act could override the rights of the dissenting creditors. *Id* at 513-14.

22. *See* text accompanying note 13 *supra*. *See generally Hearings on H.R. 4307 Before the Subcom. on Bankruptcy & Reorganization of the House Comm. of the Judiciary*, 79th Cong., 2d Sess. 15-16 (1946).

rights.[23]

The distinction between a composition and an extension has not been considered in Chapter IX litigation. Section 83(a) defines a plan of composition as including "provisions modifying or altering the rights of creditors generally."[24] Other chapters of the Bankruptcy Act deal with the difference between the two terms.[25] Most litigation has involved section 14c(5),[26] providing that a debtor may not obtain two arrangements by way of composition within a six-year period.[27] The Supreme Court in *Perry v. Commerce Loan Co.*[28] held

23. H.R. REP. NO. 2246, 79th Cong., 2d Sess. 4 (1946), *reprinted in* [1946] U.S. CODE CONG. & AD. NEWS 1246, 1249. Since the term "extension" is not mentioned in Chapter IX, it may be assumed that extensions are not prohibited. For example, cases dealing with § 14c(5), 11 U.S.C. § 32c(5), (1970) (providing that a prior discharge by composition bars another such discharge within six years) adopt this construction. *See* Perry v. Commerce Loan Co., 383 U.S. 392 (1966).

Several courts have construed § 83(i), 11 U.S.C. § 403(i) (1970). Faitoute Iron & Steel Co. v. City of Asbury Park, 316 U.S. 502 (1942); Wells Fargo Bank & Trust Co. v. Imperial Irr. Dist., 136 F.2d 539 (9th Cir. 1943), *cert. denied*, 321 U.S. 787 (1944); Leco Properties, Inc. v. R.E. Crummer & Co., 128 F.2d 110 (5th Cir. 1942); Spellings v. Dewey, 122 F.2d 652 (8th Cir. 1941); Mission Ind. School Dist. v. Texas, 116 F.2d 175 (5th Cir. 1940); West Coast Life Ins. Co. v. Merced Irr. Dist., 114 F.2d 654 (9th Cir. 1940), *cert. denied*, 311 U.S. 717 (1941); *In re* Dallas Levee Improvement Dist., 63 F. Supp. 342 (N.D. Tex. 1948); *In re* Summer Lake Irr. Dist., 33 F. Supp. 504 (D. Ore. 1940); *In re* Fort Lauderdale, 23 F. Supp. 229 (D. Fla. 1938); *In re* Drainage Dist. 7, 21 F. Supp. 798 (D. Ark. 1937); Peoples State Bank v. Imperial Irr. Dist., 15 Cal. 2d 397, 101 P.2d 466, (1940).

24. 11 U.S.C. § 403(a) (1970).

25. Some chapters, including Chapter XI, contain provisions applying to compositions and extensions alike. Other chapters, however, contain provisions which pertain only to extensions and do not mention compositions. *See, e.g.*, § 75(i), 11 U.S.C. § 203(i) (1970) (procedures for filing petitions of extension under Chapter VIII). In several cases dealing with that section, however, distinctions between the two terms were made. *In re* Mahaley, 187 F. Supp. 229 (S.D. Cal. 1960); *In re* Hoag, 62 F. Supp. 527 (D. Vt. 1945); Heldstab v. Equitable Life Assur. Soc'y., 91 F.2d 655 (10th Cir. 1937). The court in *In re Hoag*, construing § 75(k), 11 U.S.C. § 203(k), held that "[a]ltogether neither of these terms are defined by the Act, it seems to be generally assumed in the decisions that a composition is an agreement for the payment of a certain percentage of a creditor's claim in full satisfaction, while an extension contemplates an agreement extending the time within which a claim is to be paid." 62 F. Supp. at 530.

26. § 14c(5), 11 U.S.C. § 32c(5) (1970).

27. Some courts held that § 14c(5) was applicable to extensions as well as compositions. *See In re* Schlageter, 319 F.2d 221 (3d Cir. 1963); *In re* Jensen, 200 F.2d 58 (7th Cir. 1952); *In re* Fontan, 227 F. Supp. 973 (S.D. Miss. 1964); *In re* Nicholson, 224 F. Supp. 773 (D. Ore. 1963); *In re* Bingham, 190 F. Supp. 219 (D. Kan. 1960), *aff'd*, 297 F.2d 341 (10th Cir. 1961). Other courts felt that only compositions, not extensions, were barred. *See* Edins v. Helzeberg's Diamond Shops, Inc., 315 F.2d 223 (10th Cir. 1963); *In re* Holmes, 309 F.2d 748 (10th Cir. 1962); *In re* Sharp, 205 F.

that section 14c(5) does not bar an extension plan regardless of a prior discharge obtained within a six-year period in bankruptcy by way of composition.[29] The Court ruled that extension plans are different from plans of composition, finding that in the latter only part payment for the debt is contemplated. Extensions, on the other hand, do not involve a discharge in actuality since they ultimately provide for full payment of the debt.[30]

The court in *Ropico* confronted two issues. First, it addressed the applicability of the *Perry* rule to section 83(i). Second, the court faced the contention that any decrease in interest owing to the creditors would impair section 83(i) rights.[31]

The *Ropico* court, finding no Chapter IX precedents construing the extension/composition distinction, looked to both general bankruptcy law and to *Perry*.[32] The court applied the *Perry* rule, finding

---

Supp. 786 (W.D. Mo. 1962); *In re* Verlin, 148 F. Supp. 660 (E.D.N.Y. 1957), *aff'd. sub nom.* Fishman v. Verlin, 255 F.2d 682 (2d Cir. 1958). The Supreme Court resolved this conflict by finding a distinction between a composition and extension under § 14c(5). Perry v. Commerce Loan Co., 383 U.S. 392 (1966).

28. 383 U.S. 392 (1966).

29. In *Perry*, a debtor filed a petition for extension of time in which to pay his debts out of future wages. He had previously filed a petition in straight bankruptcy and obtained a discharge within six years of his second petition.

30. *Id.*

31. Plaintiffs argued that the reduction in principal from eight to six per cent made the case indistinguishable from *Faitoute* and thus in violation of § 83(i). 425 F. Supp. at 982. They also contended that the suspension of the right to receive the principal due on a short-term note amounted to an impairment of the value of the obligation, similar to a partial cancellation or surrender. *Id.* at 983.

32. The necessity and propriety of looking outside Chapter IX for guidance is an interesting issue in the case. The court apparently found the § 83(a) description of a composition inadequate to base a decision. *See* note 6 *supra*. Court decisions have made it clear that because cities are of a different status from other debtors, not all constructions of general bankruptcy law are applicable to Chapter IX. For example, Chapter IX "insolvency" is not given the same meaning under general bankruptcy law. For purposes of Chapter IX, inability to pay debts as they mature is sufficient for insolvency, while in other chapters insolvency occurs when liabilities exceed assets. *See In re* Corcoran Irr. Dist., 27 F. Supp. 322 (S.D. Cal. 1939), *aff'd. sub nom*, Newhouse v. Corcoran Irr. Dist., 114 F.2d 690 (9th Cir. 1941), *cert. denied*, 311 U.S. 717 (1941).

The court's use of general bankruptcy law may be justified in view of Congress' utilization of Chapters X and XI as models for amendments to the Municipal Bankruptcy Act in 1976. For example, provisions in the new act relating to satisfaction of claims from executory contracts, § 88(c), 11 U.S.C. § 408(c) (1976) are borrowed from Chapter X. For review of the new Chapter IX, see Bond, *Municipal Bankruptcy Under the 1976 Amendments to Chapter IX of the Bankruptcy Act*, 5 FORDHAM URB. L.J. 1 (1976); Ellison, *The Recent Revision of the Federal Municipal Bankruptcy Statute: A*

that the EMA, by calling for full payment of principal over a longer period of time, created an extension and not a composition.[33]

The court next confronted plaintiffs' assertion that the EMA created a composition despite its characterization under the *Perry* rule. Plaintiffs argued that the reduction of loan interest from eight to six per cent constituted a composition. Despite the absence of any directly relevant case law,[34] several cases involving non-interest-bearing debts provided useful direction. Plans in which no interest was provided for during the extension period were viewed as extensions.[35] The *Ropico* court reasoned that if non-interest-bearing debts may be extended without interest, the reduction to a six per cent rate contemplated by the EMA would be acceptable for the duration of the moratorium provided full interest was paid upon original maturity. The court found that since the EMA demanded full eight per cent interest payment until the maturity date, the plan was not a composition within the meaning of section 83(i).[36]

The court also considered the financial disaster facing New York City. Although the presence of such an emergency could not save an unconstitutional act, the court recognized the state's interest in aiding

---

Potential Reprieve for Insolvent Cities? 13 HARV. J. LEGIS. 549 (1976); Patchan & Collins, *1976 Municipal Bankruptcy Law*, 31 U. MIAMI L. REV. 287 (1977). The new Chapter IX does not affect the outcome of the *Ropico* case since § 83(i) was unchanged by the 1976 Amendments.

33. 425 F. Supp. at 983. Discounting special circumstances such as the reduction in interest, the distinction between the two terms here seems straightforward, and probably falls under *Perry*. *See* Flushing Nat'l Bank v. Municipal Assistance Corp., 84 Misc. 2d 976 (1975), *aff'd*, 52 App. Div. 2d 84 (1975), *rev'd on other grounds*, 40 N.Y.2d 731, 358 N.E.2d 848, 390 N.Y.S.2d 22 (1976). In *Flushing* a New York City creditor challenged the Moratorium Act under both § 83(i) and state law. *See* note 38 *infra*.

34. Plaintiffs cited *Faitoute*, in which there was no reduction in principal, noting that the § 83(i) proviso was enacted to modify that ruling. However, the court deemed *Faitoute* distinguishable since those noteholders had to accept a reduced rate of interest before and after the maturity date, while under the EMA full interest was paid up to the maturity date. 425 F. Supp. at 982-83.

35. In several cases plans were approved as extensions in which no interest was offered at all during the extension period. *See In re* Verlin, 148 F. Supp. 660 (E.D.N.Y. 1957), *aff'd sub nom.* Fisherman v. Verlin, 255 F.2d 682 (2d Cir. 1958); Heldstab v. Equitable Life Assur. Soc'y, 91 F.2d 655 (10th Cir. 1937); *In re* Mahaley, 187 F. Supp. 229 (S.D. Cal. 1960); *In re* Thompson, 51 F. Supp. 12 (W.D. Va. 1943).

36. 425 F. Supp. at 982-83. The court noted that "[i]t can be argued that the suspension of the right to receive a short-term note may in some cases be in effect an impairment of the value of the underlying obligation—similar to a partial cancellation or surrender." *Id.* at 983. In this case, however, the court found that no substantial impairment had occurred.

its cities in times of fiscal crisis.[37]

The *Ropico* court's characterization of the EMA as an extension despite its reduction of interest rates raises several problems. Although the court recognized that some plans labeled as extensions might be more appropriately termed "compositions," it made no attempt to resolve this confusion.[38] The precedents cited by the court from other chapters of the Bankruptcy Act also fail to address this question.[39] Furthermore, the *Ropico* court's reliance on cases involving non-interest-bearing debt moratoria is questionable given the interest-earning obligations involved here.[40]

The failure to clearly distinguish an extension from a composition may lie in the court's refusal to consider the effect of lower interest rates imposed on the plaintiff noteholders by the extension. The impact of inflation on creditors' rights seems relevant, given the 1975

37. The court noted that "a federal court decision that the federal Bankruptcy Act precludes the New York State legislature from implementing this emergency measure aimed at dealing with a fiscal crisis of unprecedented proportions affecting its largest city would raise very serious questions about the right of a state effectively to govern its political subdivisions." *Id.* at 984. With no binding legal precedents, the court was free to be influenced by such factors as the imminence of default.

38. 425 F. Supp. at 983. It is interesting to note that the EMA was later held to be in violation of the New York State Constitution in denying full faith and credit to the city's notes. Flushing Nat'l Bank v. Municipal Assistance Corp., 40 N.Y.2d 731, 358 N.E.2d 848, 390 N.Y.S.2d 22 (1976). *See* N.Y. CONST. art. VIII, § 2. The *Flushing* court reasoned that it was unfair to deprive short-term noteholders of remedies for three years, and that such a substantial modification of creditors' rights was prohibited by the full faith and credit clause.

Arguably the full faith and credit clause is analagous to the Bankruptcy Act's proscription against compositions on unwilling creditors: both resist substantial changes in creditors' rights which lessen the value of their notes. Perhaps the different foci of the *Flushing* and *Ropico* courts may explain their inconsistent results. In *Flushing* the court focused on the creditors' interests while the *Ropico* court looked to the city's needs. For further studies of New York City's crisis and the *Flushing* case, see Freilich, *Municipal Finance: State Courts, the Contract Clause, and the Police Power*, 9 URB. LAW. vii (1977); Note, *Municipal Corporations—a State's Police Power Does Not Allow the Alteration of the Payment Terms of Short-Term Municipal Notes*, 81 DICK. L. REV. 866 (1977); Note, *The Limits of State Intervention in a Municipal Fiscal Crisis*, 4 FORDHAM URB. L.J. 545 (1976).

39. In the cases involving § 88(c), 11 U.S.C. § 203 (1976), the composition-extension concept was not at issue. *See* note 35 *supra*.

40. All the cases cited by the court involved non-interest-bearing debts. *See, e.g., In re* Verlin, 148 F. Supp. 660 (E.D.N.Y. 1957), *aff'd. sub nom.* Fishman v. Verlin, 255 F.2d 682 (2d Cir. 1958); Heldstab v. Equitable Life Assur. Soc'y., 91 F.2d 655 (10th Cir. 1937); *In re* Mahaley, 187 F. Supp. 229 (S.D. Cal. 1960). Since there is no reduction in interest in non-interest-bearing debts, those cases are distinguishable from Ropico's interest-bearing short-term notes.

inflation rate of 9.1%.[41] At the six per cent interest rate contemplated by the EMA,[42] the noteholders would be losing money. The plaintiffs, however, failed to raise this issue.[43]

The court noted that the EMA did not impair prematurity interest,[44] yet this is not a compelling distinction. The crux of a composition is that the creditors' rights are impaired. The fact that full interest is paid until maturity of the note does not seem to be a practical distinction since creditors can lose as much in interest reduction after maturity as before maturity. Such a distinction not being determinative, the *Ropico* case could have reached either result.[45] Perhaps this best explains the refusal of the court to set any guidelines as to when a moratorium ceases to be an extension and becomes a composition.[46]

Finally, the fact that the *Ropico* court was willing to take into account the financial emergency facing New York may be of great importance to cities facing similar problems. Such consideration of financial distress is consonant with recent liberalization of the Municipal Bankruptcy Act.[47] Although the holding of the case may be re-

41. The rate of inflation reached a high of 12.7% in February 1977 and has decreased since then. U.S. Department of Labor, Bureau of Labor Statistics, Consumer Price Index (1977).

42. *See* text accompanying note 11 *supra*.

43. The court might have been able to compare the circumstances to Perry v. Commerce Loan Co., 383 U.S. 392 (1966), involving non-interest-bearing debts and an inflation rate of two to four per cent. With such a comparison, a six per cent rate would not seem unfair in the face of less than ten per cent inflation. 425 F. Supp. at 983.

44. 425 F. Supp. at 982-83.

45. The possibility of default by New York City may have been a controlling consideration in the court's decision. It seems clear that creditors' rights *were* affected in a material way and the court's distinction between *Ropico* and *Faitoute* is superfluous. Yet this distinction provided the court with a standard by which to determine the difference between a composition and an extension.

Though the decision may seem arbitrary, it is consonant with legislative trends. *See* note 47 *infra*.

46. The court recognized that the distinction between composition and extension "must at some point, because of the length of the extension or the rate of interest after maturity, become blurred." 425 F. Supp. at 983.

47. The 1976 Act relaxes the procedures for filing in bankruptcy. Before the amendments, an insolvent municipality needed consent of the creditors of 51% of its obligations before it could file in bankruptcy. § 83(a), 11 U.S.C. § 403(a) (1976). This requirement is eliminated under the 1976 Amendments. New Chapter IX also does away with the required submission of a list of the city's creditors with the petition (originally a requirement under § 83(a), since many municipal obligations are in bearer form and location of creditors is thus impractical).

stricted to emergency situations, it is a valuable precedent for other legislatures that may contemplate similar extension plans, and is an important step in the development of the law of municipal bankruptcy.[48]

Rosalynn Van Heest

Under § 82(e) of new Chapter IX, filing in bankruptcy acts as an automatic stay of all proceedings against the municipality. Prior to the recent amendments of Chapter IX, § 83(c) had provided for such stay only after filing and a hearing upon notice. A new requirement concerning creditor acceptance of the bankruptcy plan has been instituted, however, indicating that safeguards of creditors are still important. In addition, to the old requirement under § 83(d) that holders of two-thirds of the amount of claims in each class agree to the discharge, § 92(b) now mandates that over 50% of the number of claims must confirm.

Under the new Chapter IX the bankruptcy court is given authority to reject executory contracts and unexpired leases (§ 82(b)(1)), to issue certificates of indebtedness having priority over all obligations other than the city's operating expenses (§ 82(b)(2)) and to appoint a trustee for the city (§ 85(a)).

48. However, the New York City experience may lead to increased regulation of municipal securities to avoid similar occurrences in the future. At present, municipalities are subject to relatively few securities laws—the anti-fraud provisions (§ 17 of the Securities Act of 1933, 15 U.S.C. § 77g(e) and § 10(b) of the Securities Exchange Act, 15 U.S.C. § 78j(b)), and registration requirements (§ 11 of the Securities Act 15 U.S.C. § 77k). Several bills have been introduced to require greater disclosure by municipalities when issuing bonds. A House bill would amend the Securities Exchange Act to require preparation of annual reports by cities with $50 million in outstanding securities. H.R. 2724, 95th Cong., 1st Sess. 123 (1977). These would include a list of unsatisfied obligations, financial statements, and a description of the city's taxpayers. In addition to annual reports, the bill would require disclosure of both creditors' priorities and the security for the debt. For studies of municipal securities regulations and proposals, see Casey & Smith, *New Look at Municipal Bonds—Disclosure Responsibilities in the Municipal Bond Market*, 50 ST. JOHN'S L. REV. 639 (1976); Doty, *Municipal Disclosures—Recent Developments*, 9 URB. LAW. vii (1977); Doty & Peterson, *Federal Securities Laws and Transactions in Municipal Securities*, 71 NW. U. L. REV. 283 (1976); Note, *Future of Nonguaranteed Bond Financing in New York*, 45 FORDHAM L. REV. 860 (1977); Note, *Federal Regulation of Municipal Securities*, 60 MINN. L. REV. 567 (1976); Note, *Securities: Constitutional Limitations upon Federal Regulation of Municipal Issuers*, 51 ST. JOHN'S L. REV. 565 (1977); Note, *Disclosure by Issuers of Municipal Securities: An Analysis of Recent Proposals and a Suggested Approach*, 29 VAND. L. REV. 1017 (1976).