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9 UNITED STATES BANKRUPTCY COURT
 10 EASTERN DISTRICT OF CALIFORNIA
 11 SACRAMENTO DIVISION

12 In re
 13 CITY OF STOCKTON, CALIFORNIA,
 14 Debtor.

Case No. 2012-32118

D.C. No. OHS-5

Chapter 9

15 **CALPERS' MEMORANDUM**
 16 **REGARDING CONSTITUTIONAL,**
 17 **STATUTORY, AND PREEMPTION**
 18 **ARGUMENTS SUPPORTING THE**
 19 **ENFORCEABILITY OF THE PUBLIC**
 20 **EMPLOYEES' RETIREMENT LAW IN**
 21 **CHAPTER 9**

Date: October 1, 2014

Time: 10:00 a.m.

Place: Robert T. Matsui U.S. Courthouse,
 501 I Street
 Department C, Fl. 6, Courtroom 35
 Sacramento, CA 95814

Judge: Hon. Christopher M. Klein

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1 The California Public Employees’ Retirement System (“CalPERS”) files this memorandum
2 concurrently with its Supplemental Brief in Support of the City of Stockton’s First Amended Plan of
3 Adjustment (“Plan”). In that memorandum, the “Supplemental PERL Brief,” CalPERS addresses the
4 interpretation of California’s Public Employees’ Retirement Law (“PERL”). This memorandum, on
5 the other hand, addresses issues involving constitutional law, the Bankruptcy Code, and preemption
6 law, responsive to the Court’s request for briefing regarding the enforceability of specific provisions
7 of the PERL.¹

8 **I. PRELIMINARY STATEMENT**

9 The Court has raised questions regarding whether CalPERS can be impaired in a hypothetical
10 chapter 9 case, or alternatively, whether pension obligations can be adjusted. The Court has also
11 questioned whether a specific provision of the PERL, section 20487, has any effect, suggesting that
12 provision is preempted by the Bankruptcy Code. CalPERS requests that the Court refrain from
13 deciding these issues, because deciding them is unnecessary to confirmation of the City’s Plan. If the
14 Court believes it is necessary to decide these issues, the analysis below demonstrates that, while there
15 are multiple avenues to reach the same conclusion, there can be but one conclusion: a municipal
16 debtor’s obligations to CalPERS cannot be impaired or adjusted in a hypothetical chapter 9
17 bankruptcy case, and the PERL, including section 20487, is not preempted by the Bankruptcy Code.

18 **II. BACKGROUND**

19 As explained in CalPERS’ Supplemental PERL Brief, CalPERS is a State agency and, as
20 such, enjoys the sovereign rights of the State of California. The PERL (Cal. Gov. Code § 20000 *et*
21 *seq.*) establishes a retirement system for State and local government employees. *City of Oakland v.*
22 *Pub. Emps. Ret. Sys.*, 95 Cal. App. 4th 29, 33 (2002). The purpose of the PERL is to “effect economy
23 and efficiency in the public service” by providing a pension system to pay retirement compensation
24

25 ¹ For the convenience of the Court and parties in interest, CalPERS will file a separate pleading that
26 attaches the pertinent parts of exhibits and trial transcripts cited herein. In the case of transcripts, the
27 pleading(s) will attach copies of only the pages cited and surrounding pages for context as necessary.
28 In the case of declarations, the pleading(s) will attach only the declaration itself and those exhibits
referred to in the brief, rather than all exhibits to the declaration.

1 and death benefits. Cal. Gov. Code § 20001.

2 The CalPERS Board of Administration (“CalPERS Board”) has responsibility for the
3 administration of the Public Employees’ Retirement System (the “System”). The CalPERS Board is
4 governed by State statutes and the California Constitution. *City of Oakland*, 95 Cal. App. 4th at 39. In
5 1992, California voters approved Proposition 162, which gave the CalPERS Board exclusive
6 authority over the administration and investment of pension funds.² *Cal. Ass’n of Prof’l Scientists v.*
7 *Schwarzenegger*, 137 Cal. App. 4th 371, 375 (2006). In enacting Proposition 162, the electorate
8 amended article XVI, section 17 of the California Constitution, to read in part as follows:

9 Notwithstanding any other provisions of law or this Constitution to the
10 contrary, the retirement board of a public pension or retirement system shall
11 have ***plenary authority and fiduciary responsibility*** for investment of moneys
12 and administration of the system, subject to . . . the following: (a) . . . The
retirement board shall . . . have sole and exclusive responsibility to administer
the system in a manner that will assure prompt delivery of benefits and related
services to the participants and their beneficiaries.

13 (emphasis added). Proposition 162 also amended the California Constitution to provide that the
14 CalPERS Board has “the sole and exclusive power to provide for actuarial services in order to assure
15 the competency of the assets” of the System. CAL. CONST., art. XVI, § 17, subd. (e). The intent
16 behind the measure was to protect public pension funds by vesting the authority to direct actuarial
17 determinations solely with the governing board of the System. *See Direct Testimony Declaration Of*
18 *David Lamoureux In Support Of CalPERS’ Response To Franklin’s Objection To Confirmation Of*
19 *The City Of Stockton’s First Amended Plan Of Adjustment* (the “Lamoureux Decl.”) [Dkt. Nos. 1439-
20 1444], Ex. 3 at 35 (Ballot Pamp., Analysis by the Legislative Analyst, Proposition 162, Gen. Election
21 (November 3, 1992)). By granting the CalPERS Board sole authority to administer the System,
22 Proposition 162 prevents the legislative and executive branches from “raiding” pension funds to
23 balance the State budget. *Id.* at 376-37. It also prevents other outside interference with the
24 management of the System.

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27 ² The ballot pamphlet accompanying Proposition 162 explained that pension system boards should
28 give “highest priority” to providing benefits to members and their beneficiaries. Lamoureux Decl.,
Ex. 3 at 35; *City of Oakland*, 95 Cal. App. 4th at 54.

1 Cities and other public agencies³ may elect to participate in and make all or part of their
 2 employees members of the System. *See* Cal. Gov. Code § 20460. Once a city elects to participate in
 3 the System, the participating city is bound by the statutory provisions governing the System and the
 4 decisions of the CalPERS Board. Cal. Gov. Code § 20506; *City of Oakland*, 95 Cal. App. 4th at 55.
 5 Those provisions include a prohibition against failure to pay timely required employer contributions.
 6 Cal. Gov. Code § 20831. Participating cities cannot alter their funding obligations to CalPERS. *Bd. of*
 7 *Admin. v. Wilson*, 52 Cal. App. 4th 1109, 1122 (1997).⁴

8 The PERL requires a public agency contracting with CalPERS to make contributions for the
 9 public agency's employees in amounts recommended by CalPERS' actuary and approved by the
 10 CalPERS Board. Cal. Gov. Code § 20532. A public agency is also responsible to CalPERS for the
 11 expenses of determining the approximate and actual contributions, as well as of administering the
 12 System. Cal. Gov. Code §§ 20535, 20536. The PERL expressly prohibits rejection of any contract or
 13 agreement between a chapter 9 debtor and the CalPERS Board. Section 20487 provides:

14 Notwithstanding any other provision of law, no contracting agency or public
 15 agency that becomes the subject of a case under the bankruptcy provisions of
 16 chapter 9 . . . shall reject any contract or agreement between that agency and the
 board pursuant to Section 365 of Title 11 of the United States Code or any similar
 provision of law

17 Accordingly, a municipal debtor that sought to reject its relationship with CalPERS through the
 18 bankruptcy process would violate express State law. A plan of adjustment proposing to do so would
 19 not be confirmable under the Bankruptcy Code. 11 U.S.C. § 943(b)(4) (confirmation allowed only if
 20 "the debtor is not prohibited by law from taking any action necessary to carry out the plan").

21 Stockton, in its Plan, has not proposed to modify its relationship with CalPERS. Stockton has
 22 exercised its sound business judgment in reaching the conclusion that its citizens are best served by a
 23 stable and fairly compensated employee base. However, the Court has directed the parties to address
 24

25 ³ "Public agency" is generally defined in the PERL as "any city, county, district, other local authority
 26 or public body of or within this State." Cal. Gov. Code § 20056.

27 ⁴ A participating agency may elect to terminate its participation in the retirement system
 28 prospectively, but such termination does not affect contribution obligations for benefits accrued prior
 to termination. *See* Cal. Gov. Code §§ 20750, 20577.

1 the hypothetical question of whether pension obligations can be adjusted in chapter 9.

2 **III. ARGUMENT**

3 **A. A Chapter 9 Debtor Cannot Adjust its Statutory Pension Obligations to CalPERS, a**
4 **State-Run Governmental Pension System, in Violation of State Law.**

5 1. Unilateral Adjustment or Modification of a Debtor’s Obligations to CalPERS through
6 a Bankruptcy Plan Would Violate Section 903 of the Code.

7 As shown above, and in CalPERS’ Supplemental PERL Brief, the PERL imposes obligations
8 on a municipality participating in the System that are facially mandatory, whether the municipality is
9 in or out of chapter 9. These obligations cannot be set aside in a chapter 9 case because of section 903
10 of the Bankruptcy Code, which says:

11 **Section 903. Reservation of State power to control municipalities**

12 This chapter does not limit or impair the power of a State to control, by
13 legislation or otherwise, a municipality of or in such State in the exercise of the
14 political or governmental powers of such municipality, including expenditures for
15 such exercise, but—

16 (1) a State law prescribing a method of composition of indebtedness of
17 such municipality may not bind any creditor that does not consent to such
18 composition; and

19 (2) a judgment entered under such a law may not bind a creditor that does
20 not consent to such composition.

21 In section 903, Congress has expressly preserved the power of a State to control its municipal
22 creatures during the pendency of a chapter 9 case. Section 903 is the diametrical opposite of federal
23 preemption.⁵ It is an explicit instruction by Congress to the federal courts that State laws governing
24 municipalities cannot be set aside, even when State laws deal with municipal expenditures. It does
25 not even qualify the laws that may apply to expenditures. State laws may limit municipal

26 ⁵ Section 903 is not unique in federal law as an anti-preemption measure. In 1945, Congress passed
27 the McCarren-Ferguson Act, 15 U.S.C. §§ 1011-1015, to exempt the business of insurance from
28 federal regulation. In 1972 Congress enacted § 510 of the Clean Water Act, which says, “nothing in
this chapter shall . . . preclude or deny the right of any State . . . to adopt or enforce” any more
stringent limitations on the discharge of pollutants. 33 U.S.C. § 1370. Other examples exist.
McCarren-Ferguson underlies the policy that keeps federal bankruptcy courts from presiding over
insolvency cases where insurers are the petitioners. Instead, insolvent insurers come under the
supervision of State insurance commissioners in “rehabilitations” and “liquidations.” *See also* 11
U.S.C. § 109(b)(2), which aligns the Bankruptcy Code with McCarren-Ferguson.

1 expenditures, by creating debt ceilings, for example. But State laws may also mandate expenditures,
2 as the PERL does. Section 903 does not exclude either category from its scope. Section 903,
3 moreover, applies to the whole of chapter 9, including 11 U.S.C. § 901, which makes other
4 provisions of the Bankruptcy Code applicable to chapter 9 cases. Accordingly, every provision
5 which, standing alone, might be used to impair the State’s control over a municipal debtor is
6 restricted in its application by section 903.

7 A State’s consent to a municipal bankruptcy under 11 U.S.C. § 109(c)(2) does not negate
8 section 903. To say that a State waives its rights under section 903 when it consents to bankruptcy
9 would mean that section 903 would never have any effect, because State consent is required for a
10 municipality to become a debtor in chapter 9. By consenting to a chapter 9 filing by a municipality, a
11 State waives nothing, neither under the terms of the statutes nor by implication. Yet certain courts
12 have equated State consent to file for bankruptcy under section 109(c)(2) with the State ceding all
13 control over its charge during a chapter 9 case. *See, e.g., In re City of Vallejo*, 403 B.R. 72, 76
14 (Bankr. E.D. Cal. 2009). These cases are wrong. They make section 903 a nullity, which is contrary
15 to the canons of statutory construction.

16 Section 903 makes practical sense in light of 11 U.S.C. § 904, which states:

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

- 19 (1) any of the political or governmental powers of the debtor;
20 (2) any of the property or revenues of the debtor; or
21 (3) the debtor’s use or enjoyment of any income-producing property.

22 Without the preservation of State-law controls by section 903, a municipal debtor would be freed
23 from practically any constraints merely by filing a petition, because section 904 severely restricts a
24 court’s ability to interfere with the actions of a municipal debtor. Although a court cannot interfere
25 with the debtor’s use of its property by virtue of section 904, under section 903 the State *can*—“by
26 legislation or otherwise” including controlling its “expenditures.”

1 i. *Legislative History of Section 903.*

2 This construction of the meaning and effect of section 903 is not new; it is consistent with the
3 legislative history surrounding section 903 and its precursors. From the outset, Congress was aware
4 that municipal bankruptcy laws created significant potential for interference in State affairs; thus, the
5 first such law enacted in 1934 contained a provision similar to section 903. *Ashton v. Cameron Cnty.*
6 *Water Improvement Dist. No. 1*, 298 U.S. 513, 526 (1936) (quoting Section 80(k)). Legislative
7 history from the 1934 Act explains that this language was put into the law “as a further limitation
8 upon Federal power and in respect for the rights and responsibilities of the States[.]” S. COMM. ON
9 THE JUDICIARY, REP. NO. 407, at 2 (1934). Similar language was carried over into the 1937 Act,
10 which the Court upheld in *United States v. Bekins*, 304 U.S. 27 (1938).

11 In 1946, subparts (1) and (2) were added to section 903 in an effort to overrule *Faitoute Iron*
12 *& Steel Co. v. City of Asbury Park*, 316 U.S. 502 (1942), where the Court upheld a state bankruptcy
13 (composition) law regarding municipal bonds against Contract and Supremacy Clause challenges.⁶
14 At that time, Congress did not amend the operative language of that is relevant here. Congress’s
15 stated concern in adding subparts (1) and (2) was one of uniformity. H.R. REP. NO. 94-686, at 19
16 (1975), *reprinted in* 1976 U.S.C.C.A.N. 539, 557 (discussing prior legislative history of section
17 83(i)). Thus, section 903’s primary language, and its application, did not, at least in Congress’s eyes,
18 raise uniformity or Supremacy Clause concerns.

19 In the 1970s, Congress reworked federal bankruptcy laws, culminating in the creation of the
20 Bankruptcy Code in 1978. The legislative history of section 903’s precursor notes the original
21 purpose of the provision:

22 It is to prevent the statute or the court from interfering with the power
23 constitutionally reserved to the State by the Tenth Amendment. . . . ***Any State law***
24 ***that governs municipalities or regulates the way in which they may conduct their***

25 ⁶ Whether this attempted restriction on State power is constitutional given its intrusion into State
26 affairs remains an open question. *See, e.g., City of Pontiac Retired Emps. Ass’n. v. Schimmel*, 751
27 F.3d 427, 431 (6th Cir. 2014) (en banc) (questioning whether “principles of state sovereignty
28 preclude application of § 903(1)”).⁷ Although *Usery* was overruled in part by *Garcia v. San Antonio*
Metropolitan Transit Authority, 469 U.S. 528, 531 (1985), its holding is still important because it
provides the backdrop against which Congress was legislating.

1 *affairs controls in all cases. Likewise, any State agency that has been given*
 2 *control over any of the affairs of a municipality will continue to control the*
 3 *municipality in the same way, in spite of a Chapter IX petition.*

4 H.R. REP. NO. 94-686, at 19 (emphasis added). Thus, Congress intended that State laws like the
 5 PERL and State constitutional provisions would continue to control the actions of a municipal debtor
 6 during a chapter 9 proceeding.

7 During this same period, Congress was acutely aware of the Supreme Court's decision in
 8 *National League of Cities v. Usery*, in which the Court held that there are certain "attributes of
 9 sovereignty" that "may not be impaired by Congress, not because Congress may lack an affirmative
 10 grant of legislative authority to reach the matter, but because the Constitution prohibits it from
 11 exercising the authority in that manner." 426 U.S. 833, 845 (1976).⁷ Aware of the Court's
 12 "developing ideas of Federalism," Congress re-affirmed its commitment to State sovereignty by
 13 including section 903 in the Code. H.R. REP. NO. 95-598, at 262-64 (1978), *reprinted in* 1978
 14 U.S.C.C.A.N. 4717, 6220-22.^{8, 9}

15 Under the plain terms of section 903 and its legislative history (dating back to its inception),
 16 the States retain control over their political subdivisions even during a chapter 9 case. State control is
 17 so absolute that the legislative history indicates that "withdrawal of State consent at any time will
 18 terminate the case" H.R. REP. NO. 94-686, at 8, *reprinted in* 1976 U.S.C.C.A.N. 539, 545.

19 The form of control that States retain over their subdivisions varies. For example, and as
 20 explained in greater detail below, California has expressly chosen to control its municipalities in

21 ⁷ Although *Usery* was overruled in part by *Garcia v. San Antonio Metropolitan Transit Authority*,
 22 469 U.S. 528, 531 (1985), its holding is still important because it provides the backdrop against
 23 which Congress was legislating.

24 ⁸ The Court in *Usery* ultimately determined that the extension of the minimum wage and maximum
 25 hour provisions of the Fair Labor Standards Act were unconstitutional as applied to the States
 26 because "the challenged amendments operate to directly displace the States' freedom to structure
 27 integral operations in areas of traditional governmental functions" 426 U.S. at 852. During the
 28 1970s when Congress was amending the bankruptcy laws, including section 903, the legislative
 history demonstrates that certain changes were made to comport with the Court's decision in *Usery*.
 H.R. Rep. No. 95-595, at 397-98 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6353-54.

⁹ Relevant portions of legislative history cited herein will be included in the separately filed
 compendium described in footnote 1.

1 chapter 9 by preventing municipalities from rejecting their relationship with CalPERS under section
2 365 of the Bankruptcy Code. *See* Cal. Gov. Code § 20487. The fact that a municipality is in
3 bankruptcy does not alter the State’s control over the municipality through section 20487. Other
4 aspects of the PERL are of equal force and effect with respect to a municipal debtor who participates
5 in CalPERS. Congress did not intend to provide municipal debtors with a license to ignore State laws
6 governing their conduct simply because those laws may make it harder for them to adjust their debts.
7 Such adjustment cannot be done at the expense of State law. Section 903 of the Code makes this
8 clear, as do other portions of chapter 9, particularly, in the context of the confirmation decision facing
9 the court here, section 943(b)(4). By including section 903 in the Code, Congress expressed its intent
10 that the federal bankruptcy power would not be used to upset the special relationship between a
11 municipal debtor and its parent State. In this way, section 903 functions as a broad anti-preemption
12 statute, ensuring that the relationship between the municipal debtor and the State, which is protected
13 by the Tenth Amendment, is not disturbed. Section 903 ensures that state agencies like CalPERS are
14 free from interference to enforce State law with respect to a municipal debtor because State law
15 continues to be valid and not overridden merely because a chapter 9 case has been filed.

16 *ii. Uniformity.*

17 Franklin and some courts suggest that respecting State law during a chapter 9 case in
18 connection with section 903 of the Code runs afoul of Congress’s power to enact uniform laws on the
19 subject of bankruptcies. Section 903 must be applied to protect the PERL just as it does other State
20 laws governing a municipality. In any event, the suggestion demonstrates a fundamental
21 misunderstanding of the Bankruptcy Clause of the United States Constitution. *See, e.g.,* Franklin’s
22 Reply Regarding Pension Liabilities [Dkt. No. 1397] (citing *In re Cnty. of Orange*, 191 B.R. 1005,
23 1020 (Bankr. C.D. Cal. 1996)).

24 The Constitution states that Congress has the power “[t]o establish . . . uniform Laws on the
25 subject of Bankruptcies throughout the United States.” U.S. CONST. art. I, § 8, cl. 4. “The uniformity
26 requirement pertains *only* to Congress: it is an affirmative limit or restriction upon *Congress’s power,*
27 *not a limitation on the states.*” *In re Applebaum*, 422 B.R. 684, 692 (9th Cir. BAP 2009) (emphasis
28

1 added) (citing *Ry. Labor Executives' Ass'n v. Gibbons*, 455 U.S. 457, 468-69 (1982)); *see also*
2 *Gibbons*, 455 U.S. at 472 (“Bankruptcy Clause’s uniformity requirement was drafted in order to
3 prevent Congress from enacting private bankruptcy laws.”); *In re Reese*, 91 F.3d 37, 39 (7th Cir.
4 1996) (holding uniformity clause prohibits two things: (1) “arbitrary regional differences in the
5 provisions of the Bankruptcy Code”; and (2) “private bankruptcy bills—that is, bankruptcy laws
6 limited to a single debtor—or the equivalent.”).

7 Given the uniformity requirement is a limitation imposed on Congress, any claim that section
8 20487 of the PERL violates the uniformity clause fails because Congress did not pass section 20487;
9 the California Legislature did. In fact, the Supreme Court has only once invalidated an act of
10 Congress on uniformity grounds (in *Gibbons*), and that was because the act in question singled out a
11 particular railroad for particular treatment. *See In re Wetsby*, 473 B.R. 392, 405-06 (Bankr. D. Kan.
12 2012), *aff'd*, 486 B.R. 509, 515 (10th Cir. BAP 2013). By contrast, “the Uniformity Clause has never
13 been the basis for striking down a *state* enactment.” *In re Wetsby*, 473 B.R. at 407 (emphasis in
14 original). This case should not be the first.

15 Enforcing section 903 as written would also not implicate the uniformity clause. “The
16 Uniformity Clause requires that bankruptcy laws enacted by Congress be geographically uniform.”
17 *St. Angelo v. Victoria Farms, Inc.*, 38 F.3d 1525, 1531 (9th Cir. 1944) (citing *Vanston Bondholders*
18 *Protective Comm. v. Green*, 329 U.S. 156 (1946) & *Hanover Nat’l Bank v. Moyses*, 186 U.S. 181
19 (1902)); *see also In re Schaffer*, 689 F.3d 601, 610 (6th Cir. 2012) (“Rather, the Supreme Court held
20 that the laws passed on the subject of bankruptcy must be uniform throughout the United States, but
21 that uniformity is geographical, and not personal, and further stated we do not think that the provision
22 of the Bankruptcy Act as to exemptions is incompatible with this rule.”) (quoting *Moyes*, 186 U.S. at
23 188) (quotations & internal alterations omitted)). As such, “the general rule of law laid down by the
24 Supreme Court in *Moyes* was that the uniformity requirement is geographical and that variations
25 resulting from differences in state law are not unconstitutional.” *Schaffer*, 689 F.3d at 610. As the
26 Sixth Circuit said: “[S]tates and the federal government ‘have concurrent jurisdiction in bankruptcy,
27 although only Congress has the power to establish a uniform system of bankruptcy. And once
28

1 Congress passes one uniform act, if that system has differing effects on citizens based on a particular
2 state's laws, that result is acceptable.” *Id.* at 611 (quoting *In re Wetsby*, 473 B.R. at 403).

3 Any complaint that applying the plain meaning of section 903 would violate uniformity
4 concerns because of variations in the types of State laws that section 903 was designed to protect
5 rings hollow. Congress passed a uniform law in section 903. This should end the inquiry. Section 903
6 applies equally in all municipal bankruptcy cases. The fact that different States may have different
7 laws that “control” their subdivisions, and therefore the result in different cases would not be
8 uniform, is not a concern for purposes of the Bankruptcy Clause. *See, e.g., Stellwagen v. Clum*, 245
9 U.S. 605, 613 (1918) (holding that bankruptcy law may be uniform and yet “may recognize the laws
10 of the State in certain particulars, although such recognition may lead to different results in different
11 States.”); *In re Applebaum*, 422 B.R. at 692 (“The concept of uniformity requires that federal
12 bankruptcy laws apply equally in form (but not necessarily in effect) to all creditors and debtors, or to
13 ‘defined classes’ of debtors and creditors.”) (citations omitted).

14 *iii. The Constitutionality of Chapter 9 Depends on Section 903.*

15 Section 903 preserves the Bankruptcy Code from constitutional infirmity. Given the structure
16 of our Nation's constitutional design, and the control States have over their municipalities, “any
17 federal debt relief legislation affecting municipalities must be sufficiently narrow in scope to avoid
18 intrusion by the federal courts on the sovereign power of the states.” *In re Richmond Unified Sch.*
19 *Dist.*, 133 B.R. 221, 224 (Bankr. N.D. Cal. 1991). Section 903 reflects this overriding principle by
20 protecting the rights of States *qua* States to control the affairs of their political subdivisions even
21 while such subdivisions are in chapter 9. Thus, section 903 honors the long-standing principle that
22 municipalities are merely instrumentalities of the State, to which a “State may withhold, grant or
23 withdraw powers and privileges as it sees fit.” *Ysursa v. Pocatello Educ. Ass'n*, 555 U.S. 353, 362
24 (2009) (quotations omitted); *see also Ashton*, 298 U.S. at 529-30.

25 Section 903 preserves such control because it is an express limit on a municipality's ability to
26 consent to the interference of the Federal court in the internal affairs of a municipal debtor. *In re New*
27 *York City Off-Track Betting Corp.*, 434 B.R. 131, 141 (Bankr. S.D.N.Y. 2010) (“The ability of a
28

1 chapter 9 debtor to consent under section 904 is limited by section 903 of the Bankruptcy Code and
 2 federalism concerns.”); *see also In re Jefferson Cnty.*, 484 B.R. 427, 463 (Bankr. N.D. Ala. 2012); *In*
 3 *re City of Harrisburg*, 465 B.R. 744, 755 (Bankr. M.D. Pa. 2011). In other words, a municipal debtor,
 4 as a creature of state law, cannot validly even ask permission to violate State law, because of section
 5 903.

6 *Bekins* upheld the constitutionality of the 1937 revised law precisely because it protected State
 7 control over its municipalities. “The statute is carefully drawn so as not to impinge upon the
 8 sovereignty of the State. . . . The bankruptcy power is exercised . . . **only** in a case where the action of
 9 the taxing agency ***in carrying out a plan of composition*** approved by the bankruptcy court is
 10 authorized by ***state law***.” 304 U.S. at 51 (emphasis added). The Court determined that “the exercise
 11 of the federal bankruptcy power ***in dealing with a composition of the debts*** of the irrigation district,
 12 upon its voluntary application and ***with the State’s consent***,” did not violate the essential sovereignty
 13 of the State. *Id.* at 49 (emphasis added). The State must do more than simply consent to a
 14 municipality’s filing of its bankruptcy petition in order to satisfy this essential underpinning of the
 15 constitutionality of chapter 9. *Bekins* made it clear that the ***scope*** of the State’s consent includes State
 16 consent to the terms of the municipality’s plan for adjustment of debts. Section 903 is the reflection
 17 in the Code of this important principle, and it is backstopped by sections 943(b)(4) and (6), which
 18 preclude confirmation of a plan that is at variance with State law.

19 2. Unilateral Adjustment or Modification of a Municipal Debtor’s Obligations to
 20 CalPERS Through a Bankruptcy Plan Would Violate the Tenth Amendment of the
 21 United States Constitution.

22 If this Court concludes, contrary to State law, that Stockton could impair its obligations to
 23 CalPERS, it would be interjecting the federal bankruptcy power between the State and one of its
 24 subdivisions and be interfering with the State’s fiscal affairs. Thus, *in application*, chapter 9 would
 25 violate the Tenth Amendment because those two powers are reserved to the States under the Tenth
 26 Amendment.¹⁰

27 ¹⁰ The Tenth Amendment states: “The powers not delegated to the United States by the Constitution,
 28 nor prohibited by it to the States, are reserved to the States respectively, or the people.” U.S. CONST.
 amend. X.

1 As a State agency, CalPERS enjoys the sovereign rights of the State of California. The Tenth
2 Amendment reflects the “dual sovereignty” between the States and Federal government that is at the
3 heart of our Nation’s constitutional structure. *See, e.g., Gregory v. Ashcroft*, 501 U.S. 452, 457
4 (1991). Any Federal law that interferes with a sovereign function of the State, even if exercised
5 through a constitutionally delegated power, is subject to exacting scrutiny. *See, e.g., New York v.*
6 *United States*, 505 U.S. 144, 157 (1992); *Usery*, 426 U.S. at 845 (quoted above); *In re City of*
7 *Harrisburg*, 465 B.R. at 753 (“where federal bankruptcy law intersects with the rights of states to
8 regulate the activities of political subdivisions created by the state, principles of dual sovereignty as
9 defined by the Tenth Amendment must be considered.”).

10 The Tenth Amendment imposes an affirmative restriction on Congress’s powers under the
11 Bankruptcy Clause. The fact that California may have authorized its municipalities to file for chapter
12 9 protection does not mean that a federal court can interfere with the affairs between a State and one
13 of its subdivisions. The authority of the State, through its laws or otherwise, to control its political
14 subdivisions is a power reserved to the States under the Tenth Amendment and any interference with
15 that control by a bankruptcy court, or any federal court for that matter, would violate the Tenth
16 Amendment. As the Supreme Court explained:

17 Congress exercises its conferred powers subject to the limitations contained in the
18 Constitution. Thus, for example, under the Commerce Clause Congress may regulate
19 publishers engaged in interstate commerce, but Congress is constrained in the exercise
20 of that power by the First Amendment. ***The Tenth Amendment likewise restrains the***
21 ***power of Congress***, but this limit is not derived from the text of the Tenth Amendment
22 itself, which, as we have discussed is essentially a tautology. Instead, the Tenth
23 Amendment confirms that the power of the Federal Government is subject to limits
24 that may, in a given instance, reserve power to the States. ***The Tenth Amendment***
25 ***thus directs us to determine, as in this case, whether an incident of state sovereignty***
26 ***is protected by a limitation on an Article I power.***

23 *New York v. United States*, 505 U.S. at 156-57 (emphasis added). In other words, simply because
24 Congress acts pursuant to an Article I power—here, the Bankruptcy Clause—it does not mean that
25 every action taken under that enumerated power is necessarily constitutional. *Id.* at 166 (“[E]ven
26 where Congress has the authority under the Constitution to pass laws requiring or prohibiting certain
27 acts, it lacks the power to directly compel the States to require or prohibit those acts.”). Rather, such
28

1 acts and directives must also be consistent with the Tenth Amendment. *See, e.g., Alden v. Maine*, 527
2 U.S. 706, 731 (1999) (noting that Supremacy Clause “enshrines as ‘the supreme Law of the Land’
3 only those Federal Acts that accord with the constitutional design.”) (citing *Printz v. United States*,
4 521 U.S. 898, 924-25 (1997)); *see also Seminole Indian Tribe v. Florida*, 517 U.S. 44 (1996) (Article
5 I power (Indian Commerce Clause) constrained by subsequent amendment (the Eleventh)).

6 It cannot be disputed that under Federal law “[p]olitical subdivisions of States—counties,
7 cities, or whatever—never were and never have been considered as sovereign entities.” *Ysursa*, 555
8 U.S. at 362 (quoting *Reynolds v. Sims*, 377 U.S. 533, 575 (1964)). An unbroken string of cases,
9 dating back to the 1800s, recognize that municipalities are “subordinate governmental
10 instrumentalities created by the State to assist in carrying out state governmental functions.” *Id.*; *see*
11 *also City of Trenton v. New Jersey*, 262 U.S. 182, 187-90 (1923) (discussing cases); *Hunter v.*
12 *Pittsburgh*, 207 U.S. 161, 178 (1907) (citing cases); *Louisiana ex rel. Folsom v. Mayer &*
13 *Administrators of New Orleans*, 109 U.S. 285, 287 (1883). Thus, controlling the actions of political
14 subdivisions is one of the powers reserved to the States by the Tenth Amendment. As the Supreme
15 Court recognized in *Faitoute*: “The intervention of the state in the fiscal affairs of its cities is plainly
16 an exercise of its essential reserve power to protect the vital interest of its people” 316 U.S. at
17 512.

18 The court in *Ropico, Inc. v. City of New York*, recognized that sovereignty is ever-present in
19 chapter 9, and that courts presiding over chapter 9 cases must constantly walk a constitutional
20 tightrope, when it stated the following:

21 In the area of municipal reorganizations the thin line between the federal bankruptcy
22 power and state sovereignty has been particularly difficult to draw. Both Congress
23 and the Supreme Court have thus been careful to stress that the federal municipal
24 Bankruptcy Act is not in any way intended to infringe on the sovereign power of a
state to control its political subdivisions; for as the Supreme Court held in the Ashton
and Bekins cases, to the extent that the federal Bankruptcy Act does infringe on a state
or municipality’s function it is unconstitutional.

25 425 F. Supp. 970, 983 (S.D.N.Y. 1976). The provision and administration of a State pension system
26 is an incident of sovereignty, which is protected from federal intrusion in chapter 9 by the Tenth
27 Amendment and the federalism it reflects. *See, e.g., Printz*, 521 U.S. at 928 (overturning
28

1 congressional mandate to state officers and stating “[i]t is an essential attribute of the States’ retained
2 sovereignty that they remain independent and autonomous within their proper sphere of authority.”).
3 It is for this precise reason that Congress chose to exempt governmental plans, like CalPERS pension
4 plans, from Title I and IV of ERISA. *See* CalPERS’ Supplemental PERL Brief, section II.A.1. If a
5 bankruptcy court were to tinker with California’s complex statutory scheme regarding the provision
6 of public pensions under the auspices of the Bankruptcy Clause, it would be interfering in the fiscal
7 affairs of the State. This is expressly forbidden under *Bekins*.

8 Some courts, however, have suggested that by simply authorizing municipalities to file for
9 chapter 9, the authorizing State waived its sovereignty. *See, e.g., In re City of Detroit*, 504 B.R. 97,
10 150 (Bankr. E.D. Mich. 2013). This conclusion, however, rests on a misreading of the relevant
11 Supreme Court decisions. In *New York*, the Supreme Court held: “State officials thus **cannot** consent
12 to the enlargement of the powers of Congress beyond those enumerated in the Constitution.” 505
13 U.S. at 182 (emphasis added); *see also Ashton*, 298 U.S. at 531 (“The sovereignty of the state
14 essential to its proper functioning under the Federal Constitution cannot be surrendered; it cannot be
15 taken away by any form of legislation.”). The Supreme Court’s pronouncement in *New York* followed
16 on the heels of its acknowledgment that federalism, at its core, was designed “for the protection of
17 individuals.” *Id.* at 181. Despite the clarity of the Court’s language, to get around this clear language,
18 the *Detroit* court said the Supreme Court did not really mean what it said. *Detroit*, 504 B.R. at 149
19 (“states **can** ‘consent to the enlargement of the powers of Congress beyond those enumerated in the
20 Constitution.’”) (emphasis added) (quoting *New York*, but changing “cannot” to “can”).

21 Inherent in this view is an unsupportable assumption that rights emanating from the Tenth
22 Amendment belong to the States and to the States alone. Not only did *New York* reject this view, but
23 the Supreme Court recently unanimously rejected an identical argument that “States and States alone”
24 can assert a challenge that “state sovereignty” has been violated under the Tenth Amendment. *Bond*
25 *v. United States*, 131 S. Ct. 2355, 2363 (2011) (“*Bond I*”) (“Fidelity to principles of federalism is not
26 for the States alone to vindicate.”). Despite *Bond I*’s direct application, the *Detroit* court never
27 addressed *Bond I*, thus, making its analysis deficient.

1 In light of *Bond I*, the *Detroit* court’s dismissal of certain “puzzling language in *New York*” is
2 wrong. 504 B.R. at 148-49. *New York*, when read in light of *Bond I*, could not be clearer: because
3 federalism’s protections are not designed solely to protect the States alone, those rights cannot be
4 consented away by the State. A State cannot give something away that it does not solely possess. It is
5 too simplistic to say that, by authorizing one of its municipalities to file for chapter 9 protection,
6 California, or any other State, also waives its right to enforce State statutory and constitutional law
7 protecting individuals within the State, simply to benefit a single, financially distressed municipality.

8 Even assuming the protections of federalism could be consented away (which they cannot),
9 any analysis of federalism predicated on consent must consider the *scope* of such consent. Nothing in
10 California’s municipal bankruptcy authorization statute suggests a sweeping waiver of the State’s
11 sovereign control over its municipal subdivisions and its fiscal affairs. In this regard, the conclusion
12 made by the bankruptcy court in *Vallejo*—without citation to any authority—that “[w]hen a state
13 authorizes its municipalities to file a chapter 9 petition it declares that the benefits of chapter 9 are
14 more important than state control over its municipalities,” is particularly troubling. 403 B.R. at 76. In
15 essence, the *Vallejo* court held that, by merely authorizing its municipalities to file for chapter 9
16 protection, the State of California, through some unspoken “policy,” effectively gave away ***any and***
17 ***every*** measure of control that it has over its municipalities.

18 Such an interpretation improperly engrafts a “state policy” into California’s authorization
19 statute that does not appear in the statute. This conclusion makes little sense given that section 903,
20 discussed more fully above, is part of the Bankruptcy Code. Section 903 of the Code provides for
21 retention of the State’s control over a municipal debtor in chapter 9. Thus, when California
22 authorized its municipalities to file for chapter 9 it necessarily understood that it continued to
23 maintain control over its municipalities under the express terms of section 903. Nothing in the
24 authorization law provides any “clear declaration” or “unequivocal” expression that California
25 consented to have its sovereignty displaced based on the grant of authority to adjust the financial
26 affairs of a debtor through bankruptcy. On the contrary, the California Legislature expressly reserved
27 its sovereign immunity in Cal. Gov. Code § 53760.7 (the “Municipal Bankruptcy Authorization
28

1 Statute”), which the Supreme Court has indicated is an attribute of sovereignty. *Puerto Rico*
2 *Aqueduct & Sewer Auth. v. Metcalf & Eddy, Inc.*, 506 U.S. 139, 146 (1993) (“States, although a
3 union, maintain certain attributes of sovereignty, including sovereign immunity”).

4 The State of California has not consented to allow its laws regarding the administration of the
5 System to be violated by a chapter 9 debtor. CalPERS, as the statutorily and constitutionally
6 empowered arm of the State tasked with protecting the System, is making that lack of consent
7 abundantly clear. The unilateral adjustment or impairment of pensions in violation of the PERL
8 would violate the State of California’s sovereignty and would be unconstitutional under the Tenth
9 Amendment.

10 3. Section 943(b)(4) of the Bankruptcy Code Precludes Confirmation of a Plan that Does
11 Not Comply with the PERL.

12 An attempt by a municipal debtor to alter its obligations to CalPERS through the confirmation
13 of a plan of adjustment that does not comply with State law would run counter to section 943(b)(4) of
14 the Bankruptcy Code, which prohibits a plan from being confirmed “if it permits a debtor to do
15 something that is prohibited by state law” *In re Sanitary & Improvement Dist., No. 7*, 98 B.R.
16 970, 974 (Bankr. D. Neb. 1989); *see also In re City of Colorado Springs Spring Creek Gen.*
17 *Improvement Dist.*, 177 B.R. 684, 694 (Bankr. D. Colo. 1995) (“Where a plan proposes action not
18 authorized by state law, or without satisfying state law requirements, the plan cannot be confirmed.”).
19 Indeed, section 943(b)(4)’s requirement that any confirmable plan must not be inconsistent with State
20 law acts as an additional protection of State sovereignty. Thus, sections 109(c)(2), 903, 904 and
21 943(b)(4) work in harmony to protect State sovereignty and the States’ control over their political
22 subdivisions.

23 Any plan of adjustment proposing nonpayment of obligations owed to CalPERS would
24 violate Cal. Gov. Code § 20831, which states that “[n]otwithstanding any other provision of law,
25 neither the state, any school employer, nor any contracting agency shall fail or refuse to pay the
26 employers’ contribution required by this chapter or to pay the employers’ contributions required by
27 this chapter within the applicable time limitations.” Therefore, a municipal debtor’s plan would
28

1 violate section 943(b)(4) to the extent it proposed to adjust its payments to CalPERS in contravention
2 of the PERL through a plan of adjustment.

3 **B. The PERL is not Generally Preempted by the Bankruptcy Code.**

4 1. General Principles of Preemption.

5 “Federalism, central to the constitutional design, adopts the principle that both the National
6 and State Governments have elements of sovereignty the other is bound to respect.” *Arizona v.*
7 *United States*, 132 S. Ct. 2492, 2500 (2012) (citing *Gregory v. Ashcroft*, 501 U.S. 452, 457 (1991) &
8 *U.S. Term Limits, Inc. v. Thornton*, 514 U.S. 779, 838 (1995) (Kennedy, J., concurring)). Although
9 Congress has the power to preempt State law, preemption is a delicate task in light of the dual nature
10 of our constitutional design and structure. *Gonzalez v. Arizona*, 677 F.3d 383, 392 (9th Cir. 2012) (en
11 banc) (“Under our system of dual sovereignty, courts deciding whether a particular state law is
12 preempted under the Supremacy Clause must strive to maintain a ‘delicate balance’ between the
13 States and the Federal Government”) (citing *Gregory*, 501 U.S. at 460 & *Medtronic, Inc. v.*
14 *Lohr*, 518 U.S. 470, 485 (1996)), *aff’d*, *Arizona v. Inter Tribal Council of Arizona, Inc.*, 133 S. Ct.
15 2247 (2013).

16 As the Supreme Court held, there are “two cornerstones” in every preemption analysis:

17 First, the purpose of Congress is the ultimate touchstone in every pre-emption case.
18 Second, in *all* preemption cases, and *particularly in those* in which Congress has
19 legislated in a field which the States have traditionally occupied, we start with the
assumption that the historic police powers of the States were not superseded by the
Federal Act unless that was the clear and manifest purpose of Congress.

20 *Wyeth v. Levine*, 555 U.S. 555, 565 (2009) (internal citations, quotations & alterations omitted)
21 (emphasis added); *see also Pac. Gas & Elec. Co. v. California*, 350 F.3d 932, 943 (9th Cir. 2003)
22 (“*PG&E*”) (“First, we presume that Congress does not undertake lightly to preempt state law,
23 particularly in areas of traditional state regulation.”) (citations omitted). After all, the conclusion that
24 a State law is preempted is a conclusion that the State violated the Constitution’s Supremacy Clause.

25 Just last Term, the Supreme Court reaffirmed this longstanding rule stating that “[b]ecause
26 States are independent sovereigns in our federal system,’ the Court ‘assumes that the historic police
27 powers of the States were not to be superseded by the Federal Act unless that was the clear and
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1 manifest purpose of Congress.” *CTS Corp. v. Waldburger*, 134 S. Ct. 2175, 2188 (2014) ((quoting
2 *Medtronic, Inc. v. Lohr*, 518 U.S. 470, 484-85 (1996) (quoting *Rice v. Santa Fe Elevator Corp.*, 331
3 U.S. 218, 230 (1947)); *see also California v. ARC America. Corp.*, 490 U.S. 93, 101 (1989). “This
4 assumption provides assurances that ‘the federal-state balance’ will not be disturbed unintentionally
5 by Congress or unnecessarily by the courts.” *Jones v. Rath Packing Co.*, 430 U.S. 519, 525 (1977)
6 (citation omitted).

7 Most important here, the presumption against preemption applies with its greatest force when
8 the Federal law in question disrupts the relationship between a State, through its duly enacted laws,
9 and one of the State’s creatures. In such cases, the Supreme Court has cautioned that Congress does
10 not lightly, if at all, “interpos[e] federal authority between a State and its municipal subdivisions”
11 because of the total control States have over their municipal creatures. *Nixon v. Missouri Muni.*
12 *League*, 541 U.S. 125, 140 (2004); *see also Faitoute v. Iron & Steel Co. v. City of Asbury Park*, 316
13 U.S. 502, 508 (1942) (“It would offend the most settled habits in the relationship between the States
14 and the Nation to imply such a retroactive nullification of state authority over its subordinate organs
15 of government.”); *Palmer v. Massachusetts*, 308 U.S. 79, 85 (1939) (“If this old and familiar power
16 of the states [to regulate local, intrastate railroad services] was withdrawn when Congress gave
17 district courts bankruptcy powers over railroads, we ought to find language fitting for so drastic a
18 change.”).

19 Chapter 9 cases are different than cases brought under other chapters of the Bankruptcy Code
20 because of the relationship between a city and a State. *See e.g., In re City of San Bernardino*, 2014
21 WL 2511096, at *12 (C.D. Cal. June 4, 2014) (“Municipal bankruptcies implicate a state’s
22 sovereignty and Tenth Amendment rights to a greater degree than other bankruptcy contexts because
23 of the special relationship between a state and its municipalities.”); *In re City of Colorado Springs*
24 *Spring Creek Gen. Improvement Dist.*, 177 B.R. 684, 693 (Bankr. D. Colo. 1995) (“The bankruptcy
25 of a public entity is different from that of a private person or concern. Unlike any other chapter of the
26 Bankruptcy Code, Chapter 9 places federal law in juxtaposition to the rights of states to create and
27 govern their own subdivisions.”). *Cf. City of Trenton v. New Jersey*, 262 U.S. 183, 185 (1923) (“The
28

1 relations existing between the state and the water company were not the same as those between the
 2 state and the city.”). Because municipalities are created by State law, and exist to perform State
 3 functions at the local level, courts must invoke a “working assumption that federal legislation
 4 threatening to trench on the States’ arrangements for conducting their own government should be
 5 treated with *great skepticism*, and read in a way that preserves a State’s chosen disposition of its own
 6 power, in the absence of the plain statement *Gregory* requires.” *Nixon*, 541 U.S. at 140 (emphasis
 7 added).

8 As for bankruptcy in general, “[e]ven though bankruptcy is one of only two federal legislative
 9 powers in Article 1, Section 8 of the Constitution in which the power to make ‘uniform’ law is made
 10 explicit, the presumption against displacing state law by federal bankruptcy law is just as strong in
 11 bankruptcy as in other areas of federal legislative power.” *PG&E*, 350 F.3d at 943 (discussing
 12 *Midlantic Nat’l Bank v. New Jersey Dep’t of Envtl. Prot.*, 474 U.S. 494, 501 (1986) & *BFP v.*
 13 *Resolution Trust Corp.*, 511 U.S. 531 (1994)). As the Supreme Court explained:

14 Federal statutes impinging upon important state interests cannot be construed
 15 without regard to the implications of our dual system of government. When the
 16 Federal Government takes over local radiations in the vast network of our national
 17 economic enterprise and thereby radically readjusts the balance of state and
 18 national authority, those charged with the duty of legislating must be reasonably
 explicit. . . . ***To displace traditional state regulation in such a manner, the
 federal statutory purpose must be clear and manifest.*** Otherwise, the Bankruptcy
 Code will be construed to adopt, rather than displace, pre-existing state law.

19 *BFP*, 511 U.S. at 544-545 (citations omitted) (emphasis added); *see also Gregory*, 501 U.S. at 460-61
 20 (“If Congress intends to alter the usual constitutional balance between the States and the Federal
 21 Government, it must make its intention to do so unmistakably clear in the language of the statute. . . .
 22 Congress should make its intention clear and manifest if it intends to pre-empt the historic powers of
 23 the States.”) (quotations and citations omitted).¹¹

24
 25 ¹¹ *Gregory* is a major federalism case. In *Gregory*, one of the issues before the Court was whether
 26 the State of Missouri’s mandatory retirement requirement for judges violated the Federal Age
 27 Discrimination in Employment Act (“ADEA”), which was passed pursuant to Congress’s Commerce
 28 Clause power under Article 1, section 8 of the Constitution. Given the federalism concerns, the Court
 employed the “plain statement rule” in interpreting the ADEA to avoid a reading of the statute that
 would intrude upon the sovereignty of the State of Missouri. 501 U.S. at 464 (“Application of the
 plain statement rule thus may avoid a potential constitutional problem.”); *see also id.* at 461

1 There are three forms of preemption: (1) express preemption, (2) field preemption, and
2 (3) conflict preemption. *Arizona v. United States*, 132 S. Ct. 2492, 2500-01 (2012) (citations
3 omitted). As noted, the touchstone of any preemption analysis is congressional purpose. None of
4 these three types of Federal preemption can apply here because of the express anti-preemption
5 provision of section 903, but the following analysis shows that preemption does not occur in any
6 event.

7 With respect to express preemption, there is no language in the Bankruptcy Code that
8 expressly preempts the PERL. *Compare* 11 U.S.C. § 365(a) *with Riegel v. Medtronic, Inc.*, 552 U.S.
9 312, 316 (discussing 21 U.S.C. § 360k(a), which contained an “express preemption provision” that
10 said, in part, “no State or political subdivision of a State may establish . . .”).

11 Equally meritless is any notion that the Bankruptcy Code amounts to “field preemption,” of
12 the PERL as confirmed by the unequivocal pronouncements of the Supreme Court and the Ninth
13 Circuit. *Midlantic*, 474 U.S. at 505 (“Congress did not intend for the Bankruptcy Code to pre-empt all
14 state laws.”); *see also In re Tippett*, 542 F.3d 684, 689-690 (9th Cir. 2008) (concluding that
15 Bankruptcy Code does not field-preempt a State statute protecting bona fide purchasers of real estate;
16 *In re Miles*, 430 F.3d 1083, 1092 (9th Cir. 2005) (“it cannot be said that Congress has completely
17 preempted all state regulation which may affect the actions of parties in bankruptcy court”)
18 (quotation and citation omitted); *In re Applebaum*, 422 B.R. at 689 (9th Cir. BAP 2009) (“Federal
19 bankruptcy law is not so pervasive, nor is the federal interest so dominant, as to wholly preclude state
20 legislation in the area.”). Thus, there is no field preemption of the PERL.

21 As explained in greater detail below, there is likewise no “conflict preemption” of the PERL.
22 The PERL does not conflict with chapter 9, nor stand as an obstacle to its purposes. Even if there
23 were a conflict by implication or in application of one or the other, section 903 explicitly preserves
24 State law, as discussed at other points in this brief.

25
26
27 (explaining that “plain statement rule” and “clear and manifest” rule are virtually the same and both
28 derive from the recognition that “States retain substantial sovereign powers under our constitutional
scheme, powers with which Congress does not readily interfere.”).

1
2 **C. California Government Code § 20487 is Constitutionally Valid and is Not Preempted by**
3 **Section 365 of the Bankruptcy Code.**

4 Although the City has not sought to reject, assume or assign its CalPERS contract, and
5 Franklin has not made any real pre-enforcement challenge to section 20487 of the PERL in this case,
6 the Court has queried whether section 20487 is valid. Hr'g Tr. 47:5-7, June 8, 2014. Section 20487 is
7 a valid exercise of the California's Legislature's sovereign control over its political subdivisions and
8 should be respected in a chapter 9 case.

9 The Court appears to direct CalPERS to address the issue of whether section 20487 is
10 unconstitutional on its face, as preempted by federal law. An opinion of the Court on the facial
11 validity of section 20487 would constitute a de facto declaratory judgment against the State of
12 California with respect to the validity of one of its statutes. Both the Supreme Court and the Ninth
13 Circuit have recognized that special care must be taken when a court issues a declaratory judgment
14 against a sovereign defendant:

15 Declaratory proceedings in the federal courts against state officials must be decided
16 with regard to the implications of our federal system. . . . Anticipatory judgment by a
17 federal court to frustrate action by a state agency is even less tolerable to our
18 federalism. . . . The procedures of review usually afford ample protection to a carrier
whose federal rights are actually invaded. . . . State courts are bound equally with the
Federal Courts by the Federal Constitution and laws.

19 *Exxon Shipping Co. v. Airport Depot Diner, Inc.*, 120 F.3d 166, 170 (9th Cir. 1997) (quoting *Pub.*
20 *Serv. Comm'n v. Wycoff Co., Inc.*, 344 U.S. 237, 247-48 (1952)).

21 The Supreme Court has consistently acknowledged that a facial challenge to a statute is “the
22 most difficult challenge to mount successfully” because “the challenger must establish that no set of
23 circumstances exists under which the [statute] would be valid.” *United States v. Salerno*, 481 U.S.
24 739, 745 (1987); *see also Anderson v. Edwards*, 514 U.S. 143, 155 n.6 (1995) (applying *Salerno*
25 standard in a preemption case). Thus, for this Court to conclude that section 20487 is preempted and
26 therefore facially unconstitutional, it must decide that under no set of circumstances can this law
27 survive judicial scrutiny. As for the burden of proof, the party claiming preemption bears the
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1 burden¹² of proving that “no set of circumstances exist.” *See, e.g., Silkwood v. Kerr-McGee Corp.*,
 2 464 U.S. 238, 255 (1984). It is against these principles that any claim of preemption must be
 3 analyzed.

4 1. Section 20487 Is Part of the State’s “Consent” to File for Chapter 9 Protection.

5 The Bankruptcy Code provides that “an entity may be a debtor under chapter 9 of this title if
 6 and only if such entity . . . is specifically authorized . . . to be a debtor under such chapter by State
 7 law . . .” 11 U.S.C. § 109(c)(2). There is no inherent right of any municipality to be a chapter 9
 8 debtor, because States act as the gatekeepers to a municipality’s entry into chapter 9. *See, e.g., In re*
 9 *City of Harrisburg, Pa.*, 465 B.R. 744, 754-55 (Bankr. M.D. Pa. 2011); *In re City of Stockton*, 475
 10 B.R. 720, 728-29 (Bankr. E.D. Cal. 2012) (“*Stockton I*”); *In re City of Stockton*, 478 B.R. 8, 17
 11 (Bankr. E.D. Cal. 2012) (“*Stockton II*”) (noting states “may control the prerequisites for consenting”
 12 to a chapter 9 filing). This is so because the relationship between a State and one of its subdivisions is
 13 safeguarded by the Tenth Amendment to the United States Constitution. *See In re City of Harrisburg*,
 14 465 B.R. at 754 (“Congress amended § 109(c)(2) to clarify that a state must provide ‘specific’
 15 authorization to comply with Tenth Amendment constraints.”); *see also Faitoute*, 316 U.S. at 512
 16 (“The intervention of the state in the fiscal affairs of its cities is plainly an exercise of its essential
 17 reserve power to protect the vital interests of its people . . .”). While some States expressly prohibit
 18 their subdivisions from filing for chapter 9 or are silent on the matter,¹³ other States, like California,
 19 place restrictions on the entry to chapter 9. Thus, it is undisputed that States have total control over
 20 whether or not their municipalities can file for chapter 9.

21 Franklin concedes as much. *See Franklin’s Reply Regarding Pension Liabilities*, p. 3 [Dkt.
 22 No. 1397] (“There is no question that, absent state consent, the Tenth Amendment prohibits a
 23 municipality from seeking bankruptcy protection . . .”) (emphasis in original). While CalPERS

24 _____
 25 ¹² Here, there does not appear to be a party claiming preemption of section 20487, making it unclear
 26 who bears the burden of proof. Certainly, if the party claiming preemption were Franklin, it has not
 met the burden.

27 ¹³ *See, e.g.,* MARC A. LEVINSON, ET AL., MUNICIPALITIES IN PERIL, THE ABI GUIDE TO CHAPTER 9 75-
 28 88 (listing known State municipal bankruptcy authorization laws).

1 agrees that this is an accurate statement of the law, Franklin’s citation to the Supreme Court’s
2 decision in *Ashton* as the genesis for this conclusion reveals Franklin’s misunderstanding of the law.

3 In *Ashton*, the lack of a State “consent” mechanism was not the reason the Court struck down
4 the first municipal bankruptcy law, contrary to Franklin’s claim. The opposite is true. The act in
5 question contained a “consent” provision and the State of Texas passed a law authorizing its
6 municipalities to file for bankruptcy protection. *Id.* at 526 (quoting § 80(k), which provided that
7 States had the “power to require the approval by any governmental agency of the State of the filing of
8 any petition hereunder and of any plan of readjustment); *id.* at 527 (noting Texas law authorizing
9 filing). Rather, the Supreme Court struck down the law because it interfered with the relationship
10 between a State and one of its political subdivisions. The Supreme Court held:

11 If obligations of states or their political subdivisions may be subjected to the
12 interference here attempted, they are no longer free to manage their own affairs; the
13 will of Congress prevails over them And really the sovereignty of the state, so
14 often declared necessary to the federal system, does not exist.

14

15 Neither consent nor submission by the states can enlarge the powers of Congress; none
16 can exist except those which are granted. The sovereignty of the state essential to its
17 proper functioning under the Federal Constitution cannot be surrendered; it cannot be
18 taken away by any form of legislation.

17 *Id.* at 531 (internal citations omitted).

18 Further, if Franklin were correct, the Supreme Court would not have upheld Congress’s
19 second attempt at a municipal bankruptcy law because that law **did not** have any mechanism for State
20 consent. *United States v. Bekins*, 304 U.S. 27, 49 (1938) (discussing differences between former
21 section 80(k) and new section 83(i)). *See also* David L. Dubrow, *Chapter 9 of the Bankruptcy Code:
22 A Viable Option for Municipalities in Fiscal Crisis?*, 24 Urb. Law 539, 551 (1992) (arguing that the
23 Supreme Court’s composition was the key to the about-face in *Bekins* because the new “Chapter 10
24 was in one respect weaker than Chapter 9 with respect to state sovereignty. While Chapter 9 required
25 state consent for a municipality to file for relief, Chapter 10 did not do so.”). In fact, the *Bekins* court
26 deemed the fact that the law did not require the consent of the parent State to file for bankruptcy to be
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1 “immaterial.” *Bekins*, 304 U.S. at 49.¹⁴ Thus, Franklin grossly overstates the doctrinal point by
2 claiming that State consent was the *sine qua non* of the Court’s holdings in *Ashton* and *Bekins*.
3 Franklin’s Reply Regarding Pension Liabilities, p. 3.

4 Rather, the Court made it clear that it was upholding the revised municipal bankruptcy law
5 not because the State had consented, but because:

6 The statute is carefully drawn so as not to impinge on the sovereignty of the State.
7 The *State retains control of its fiscal affairs*. The bankruptcy power is exercised in
8 relation to a matter normally within its province and *only in a case where the action
of the taxing agency in carrying out a plan of composition approved by the
bankruptcy court is authorized by state law*.

9 *Bekins*, 304 U.S. at 51 (emphasis added). In other words, both *Ashton* and *Bekins* were predicated on
10 the notion that federal courts should not interfere with the States and their creatures and that
11 municipal debtors would continue to comply with State laws while they were in bankruptcy. *See, e.g.*,
12 *Ropico*, 425 F. Supp. 970, 983 (S.D.N.Y. 1976). Indeed, scholars at the time noted that, far from
13 undermining *Ashton*’s non-interference principles, *Bekins* reaffirmed that principle. *See also* Giles J.
14 Patterson, *Municipal Debt Adjustment Under the Bankruptcy Act*, 90 U. PA. L. REV. 520, 531 (1942)
15 (“The court can make no order that will even indirectly interfere with the sovereignty of the state, nor
16 compel action by the debtor. The *Bekins* case did not reverse this principle of constitutional law
17 announced in the *Ashton* case. It reaffirmed it.”).

18 There is no doubt that State limitations on a municipality’s powers in bankruptcy are
19 constitutional given that political subdivisions are mere creatures of State law. Their existence,
20 powers, duties, constraints and attributes are functions of State law. In fact, State control is so
21 absolute that the legislative history of chapter 9 indicates that “withdrawal of State consent at *any*
22 *time* will terminate the case” H.R. REP. NO. 94-686, at 8, *reprinted in* 1976 U.S.C.C.A.N. 539,
23 545 (emphasis added). Thus, simply because a court had already determined that a municipal debtor
24 was eligible, does not mean that the eligibility decision is not subject to revision at any time, because
25 the State could withdraw its consent to remain in chapter 9 at any time during the pendency of the
26

27 ¹⁴ In *Bekins* the State of California did in fact consent to the filing via an authorization statute.
28 *Bekins*, 304 U.S. at 47.

1 bankruptcy proceedings. *Cf. In re Richmond Unified Sch. Dist.*, 133 B.R. 221, 223-26 (Bankr. N.D.
2 Cal. 1991) (chapter 9 debtor, under influence of State, has unqualified right to dismiss chapter 9 case
3 over objection of creditors). If a municipal debtor chose to reject its relationship with CalPERS under
4 section 365, it would be in direct contravention of a specific limitation that California placed on its
5 political subdivision's entry into chapter 9. If a municipality chose to seek to reject its relationship
6 with CalPERS, it would no longer be eligible for chapter 9. And, as the legislative history above
7 confirms, this would be completely consistent with Congress's intent because a State can withdraw
8 its "consent at any time" during the pendency of the chapter 9 proceeding and doing so "will
9 terminate the case."

10 2. California's Municipal Bankruptcy Authorization Statute, Cal. Gov. Code § 53760,
11 Did Not Repeal Section 20487 of the PERL.

12 California's municipal bankruptcy authorization law, Cal. Gov. Code § 53760, which became
13 effective on January 1, 2012, provides:

14 A local public entity in this state may file a petition and exercise powers pursuant to
15 applicable federal bankruptcy law if either of the following apply:

16 (a) The local public entity has participated in a neutral evaluation process pursuant
17 to Section 53760.3.

18 (b) The local public entity declares a fiscal emergency and adopts a resolution by a
19 majority vote of the governing board pursuant to Section 53760.5.

20 It is noteworthy that the introductory paragraph of the authorization statute does not say that a local
21 public agency can exercise *all* powers under the Federal bankruptcy law. By referencing "applicable"
22 bankruptcy law, the authorization constrains the debtor to operate within the confines of section 903
23 and, at plan confirmation, sections 943(b)(4) and (6). Indeed, section 53760.7 expressly notes that the
24 State did not waive its immunity from suit in federal court by authorizing its municipalities to file for
25 chapter 9. While the State's authorization for filing is broad, it is not a blanket delegation of authority
26 to the State's creatures.

27 Section 20487 of the PERL, which was originally enacted in 1996, long before the municipal
28 bankruptcy authorization law, states:

1 ***Notwithstanding any other provision of law***, no contracting agency or public agency
 2 that becomes the subject of a case under the bankruptcy provisions of Chapter 9
 3 (commencing with Section 901) of Title 11 of the United States Code shall reject any
 4 contract or agreement between the agency and the board pursuant to Section 365 of
 5 Title 11 of the United States Code or any similar provision of law; nor shall the
 6 agency, without prior written consent of the board, assume or assign any contract or
 7 agreement between that agency and the board pursuant to Section 365 of Title 11 of
 8 the United States Code or any similar provision of law.

9 (emphasis added). Given its singular focus, this statute is a ***specific*** statute. Moreover, the
 10 emphasized “notwithstanding” phrase means what it says. *Watkins v. Cnty. of Alameda*, 98 Cal. Rptr.
 11 3d 847, 866 (2009) (“The clause means what it says.”). As the California Court of Appeals said:
 12 “‘Notwithstanding’ means ‘without prevention or obstruction from or by’ or ‘in spite of’ or
 13 ‘despite.’” *Klajic v. Castaic Lake Water Agency*, 16 Cal. Rptr. 3d 746, 751 (2004) (quoting
 14 dictionaries) (emphasis in original). The phrase is a “term of art that declares the legislative intent to
 15 override all contrary law. By use of this term, the Legislature expresses its intent to have the specific
 16 control despite the existence of other law which ***might*** otherwise govern.” *Id.* (citations & quotations
 17 omitted) (emphasis added); *see also In re Marriage of Cutler*, 94 Cal. Rptr. 2d 156, 166 (2000) (“The
 18 phrase ‘notwithstanding any other provision of law’ is a very comprehensive phrase. This phrase
 19 signals a broad application ***overriding all other code sections*** unless it is specifically modified by use
 20 of a term applying it only to a particular code section or phrase.”) (emphasis added).

21 Here, the Court must analyze the interplay between section 20487 and section 53760, two
 22 California statutes both located in the Government Code. Because it is construing two California
 23 statutes, the Court must apply California’s rules regarding statutory interpretation. *Powell’s Books*
 24 *Inc. v. Kroger*, 622 F.3d 1202, 1209 (9th Cir. 2010) (Federal courts interpreting State statutes apply
 25 State rules of statutory construction). Since no controlling decision from the California Supreme
 26 Court exists interpreting the interplay between these two statutes, this Court must “predict” how the
 27 California Supreme Court would interpret these two laws in conjunction with one another. *See, e.g.,*
 28 *In re Kirkland*, 915 F.2d 1236, 1239 (9th Cir. 1990).

 There are several statutory construction rules that come into play here:

(1) The “‘ultimate task’ in statutory interpretation ‘is to ascertain the legislature’s intent.’”
In re First T.D. & Investment, Inc., 253 F.3d 520, 527 (9th Cir. 2001) (quoting *People v. Massie*, 19

1 Cal. 4th 550, 569 (1998)).

2 (2) “[W]hen two statutes relate to the same subject, the more specific one will control
3 unless they can be reconciled.” *Royalty Carpet Mills, Inc. v. City of Irvine*, 23 Cal. Rptr. 3d 282, 287
4 (2005) (collecting cases).

5 (3) “When the two statutes can be reconciled, they must be construed in reference to each
6 other, so as to harmonize the two in such a way that no part of either becomes surplusage.” *Id.*
7 (quotation omitted).

8 (4) Repeals by implication are strongly disfavored. *W. Oil & Gas Ass’n v. Monterey Bay*
9 *Unified Air Pollution Control Dist.*, 49 Cal. 3d 408, 419-20 (1989).

10 (5) If there is a “reasonable construction of a statute which avoids constitutional
11 infirmity” courts applying California law “must adopt that construction.” *Cent. Delta Water Agency*
12 *v. State Water Res. Control Bd.*, 21 Cal. Rptr. 2d 453, 463 (1993). A corollary to this is the rule of
13 construction providing that California courts will not decide constitutional issues unless absolutely
14 necessary. *See, e.g., Palermo v. Stockton Theatres, Inc.*, 32 Cal. 2d 53, 65 (1948) (“We are of the
15 view that this issue, unnecessary to our decision, should not be decided here or made the subject of
16 dictum.”). Likewise, California courts will interpret statutes to avoid even raising constitutional
17 issues. *See id.* at 60 (“A like duty requires us to avoid a construction which raises grave and doubtful
18 constitutional questions if the statute can reasonably be construed so as to avoid such questions.”)
19 (quotation omitted).

20 Applying these rules of statutory construction, it becomes apparent that section 20487 must be
21 construed as part of the State’s consent to file a chapter 9 case. The broad “notwithstanding” phrase,
22 as a matter of California law, demonstrates that the California Legislature made its intentions clear:
23 regardless of any other law, a California municipal debtor cannot reject its contract with CalPERS or
24 assign or assume such a contract without the CalPERS Board’s consent. Thus, while California
25 generally authorized its municipalities to file for chapter 9, it expressly prohibited them from
26 rejecting their contracts with CalPERS. The legislative intent is clear. Both section 20487 and section
27 53760 relate to the same subject: municipal bankruptcy. As a result, the more specific statute (section
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1 20487) must control over the general (section 53760). The two statutes can easily be reconciled.
2 Section 53760 is a general authorization statute, while section 20487 is an exception to this general
3 authorization. In this regard, another rule of California statutory construction becomes important. The
4 California Legislature is deemed to be aware of its own laws when enacting new laws. *Shirk v. Vista*
5 *Unified Sch. Dist.*, 42 Cal. 4th 201, 212 (2007) (“The Legislature is deemed to be aware of existing
6 statutes, and we assume that it amends a statute in light of those preexisting statutes.”). Thus, if the
7 California Legislature had desired that its creatures could use chapter 9 to reject CalPERS contracts,
8 it would have directly repealed section 20487. There is no question it did not.

9 Franklin has suggested that the California Legislature implicitly repealed section 20487 when
10 it enacted section 53760. Franklin’s Reply Regarding Pension Liabilities, p. 6-7. This is contrary to
11 California law. California law imposes a strong presumption against implied repeal. The presumption
12 against implied repeal is so strong that, “[t]o overcome the presumption the two acts must be
13 irreconcilable, clearly repugnant, and so inconsistent that the two cannot have concurrent operation.”
14 *W. Oil & Gas*, 49 Cal. 3d at 419 (quotations omitted). Courts are bound “to maintain the integrity of
15 both statutes if the two may stand together. There must be *no possibility* of concurrent operation.” *Id.*
16 at 419-420 (quotations omitted) (emphasis in original). Moreover, “Courts have also noted that
17 implied repeal should not be found unless the later provision gives *undebatable evidence* of an intent
18 to supersede the earlier provision.” *Id.* at 420 (emphasis in original) (internal quotations & alterations
19 omitted). *Accord Morton v. Mancari*, 417 U.S. 535, 550-51 (1974). Here, there is no evidence, let
20 alone “undeniable evidence,” evincing any intent on behalf of the California Legislature that section
21 20487 was repealed by section 53760. Indeed, the two statutes coexist quite peacefully.

22 Simply predicating a political subdivision’s entry into chapter 9 on a condition—that a
23 municipal debtor cannot reject its contract with CalPERS—does not nullify section 53760. In fact,
24 this case proves the point. The City, without seeking to reject its relationship with CalPERS, has
25 consensually compromised with all of its creditors, save one. And, its Plan sets it on a course of fiscal
26 stability into the foreseeable future. In that sense, section 53760 has achieved its purposes without
27 doing violence to section 20487. Under California law, this Court must determine whether the two
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1 statutes can “stand together.” The evidence at trial demonstrates that the two laws easily “stand
2 together” and the operation of one is not so “irreconcilable, clearly repugnant, and so inconsistent that
3 the two cannot have concurrent operation.” *W. Oil & Gas* at 419-20. Accordingly, the municipal
4 bankruptcy authorization statute did not implicitly repeal section 20487.

5 The legislative history of section 20487 also makes clear that the California Legislature
6 viewed section 20487’s prohibition on rejection as part of its “consent” to allow California’s political
7 subdivisions to *file* for chapter 9 protection. For example, numerous portions of the legislative history
8 of section 20487 reference how other States have placed “conditions on the right to seek bankruptcy
9 relief.” *See, e.g.,* Legislative History Research Report Regarding Cal. Gov. Code § 20487, pp. 25-27.
10 Likewise, the legislative history of section 20487 specifically references the fact that the State has the
11 authority to require “preconditions for filing a Chapter 9 bankruptcy.” *See, e.g., id.* at p. 59, 89, 97,
12 184. Further, the legislative history of section 20487 specifically references California’s former
13 authorization statute on several occasions. *See, e.g., id.* at 26. This is all probative evidence of the
14 California Legislature’s intent and this evidence tilts sharply in favor of finding that section 20487 is
15 part and parcel of California’s authorization statute and part of the “consent” the State of California
16 has given its municipalities to file for chapter 9.

17 Based on all of this, it is well within reason to construe section 20487 as part of California’s
18 consent to allow its municipalities to file for chapter 9. After all, this Court’s task under the
19 California statutory construction principles set forth above is not to conclude that such a construction
20 is the best one, but only a “reasonable” one or one that is “fairly debatable.” *Cent. Delta Water*, 21
21 Cal. Rptr. 2d at 463; *CalFarm Ins. Co. v. Deukmejian*, 48 Cal. 3d 805, 814-15 (1989) (“If the validity
22 of the measure is ‘fairly debatable,’ it must be sustained.”). This is premised on the fact that, under
23 California law, “statutes are not presumed unconstitutional unless proven constitutional, but rather
24 the reverse.” *Cent. Delta Water*, 21 Cal. Rptr. 2d. at 463 (citing *CalFarm Ins.*). Consequently, in
25 making its “prediction” on what the California State Supreme Court would say on the matter, this
26 Court must conclude that section 20487 is part of the State’s consent to authorize the filing of a
27 chapter 9 petition by one of its creatures.

1 3. Section 20487 Is Protected by Section 903 of the Code and Is Not Preempted by the
2 Bankruptcy Code.

3 Section 20487 of the PERL is the type of law that section 903 of the Bankruptcy Code was
4 designed to protect from preemption because it reflects the State of California's control over its
5 municipalities' governmental and political powers. As such, under the express will of Congress as
6 reflected in section 903, section 20487 must stand. Furthermore, there is no indication that Congress,
7 by enacting section 365, clearly and manifestly intended to preempt section 20487. In fact, given the
8 history and context of chapter 9 the opposite is true.

9 i. *Section 20487 Is Protected From Preemption By Section 903.*

10 Through section 903 Congress created a constitutional boundary between the bankruptcy
11 court, the debtor and the State. Its command could not be clearer, as it is prefaced with the phrase
12 "This chapter does not limit or impair the power of the State . . ." The phrase "this chapter"
13 obviously means chapter 9, and by incorporation through section 901, section 365 of the Code. Thus,
14 the powers granted to a municipal debtor in bankruptcy are limited by section 903. That is clear from
15 the face of the statute. Section 20487 falls well within the ambit of the requirement that a State is able
16 to control the "political and governmental powers of such municipalities" during a chapter 9 case.

17 Under Cal. Gov. Code § 45341, a city may establish a pension plan "in order to effect
18 economy and efficiency in the public service," which are the same goals expressed by the California
19 Legislature when it created the State retirement system. Cal. Gov. Code § 20001. The Stockton
20 Charter mandates that the City "provide for a retirement and death benefit plan for officers and
21 employees of the City." Stockton City Charter Art. XXVI, § 2600; *see also id.* at § 2601 ("The City
22 Council may provide for such a plan by participation in any retirement system and death benefit plan
23 now existing or hereafter created under the laws of the State of California which municipalities and
24 municipal officers and employees are eligible to join."). "The authority to provide for pensions . . .
25 [is] a municipal affair." *Richards v. Wheeler*, 10 Cal. App. 2d 108, 111 (1935) (citing cases); *see also*
26 *Bellus v. City of Eureka*, 69 Cal. 2d 336, 345 (1968) ("The City here agrees that establishment of an
27 employee pension plan is a municipal affair."). The California Supreme Court has recognized that the
28 term "municipal affairs" encompasses "governmental activity." *Cal. Fed. Savings & Loan Ass'n v.*

1 *City of Los Angeles*, 54 Cal. 3d 1, 17-18 (1991). Thus, by providing for pension benefits, the City is
2 exercising one of its “political or governmental powers” as envisioned in section 903. *See* M.
3 McConnell & R. Picker, *When Cities Go Broke: A Conceptual Introduction to Municipal*
4 *Bankruptcy*, 60 U. Chi. L. Rev. 425, 462-63 (1993) (“The application [of § 903] to only political or
5 governmental powers seems to recognize the traditional distinction in local government law between
6 proprietary and nonproprietary activities of municipalities. . . . This may or may not have any
7 practical significance, because the governmental/proprietary distinction has all but collapsed”).

8 Stockton chose to participate in CalPERS. *See* Cal. Gov. Code § 45345. By doing so, it
9 agreed to be bound “to all provisions of this part and all amendments thereto.” Cal. Gov. Code §
10 20506. This, of course, includes section 20487 of the PERL. Thus, given that pensions are considered
11 to be a governmental function as a matter of both Federal (*see* CalPERS’ Supplemental PERL Brief),
12 and State law, by agreeing to participate in CalPERS, Stockton expressly ceded this particular
13 governmental function back to the State through its agency, CalPERS.¹⁵ As such, it has no right to
14 reject its relationship with CalPERS via the Bankruptcy Code because section 903 expressly prohibits
15 interference with the State’s ability to control its municipalities in the exercise of its political or
16 governmental powers.

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18 ¹⁵ The concept that the provision and administration of a public pensions system is a governmental
19 function has been recognized by several other courts. *See, e.g., Crosby v. City of Gastonia*, 682 F.
20 Supp. 2d 537, 546 (W.D.N.C. 2010) (“the act of funding the [Gastonia Supplementary Pension Fund]
21 would be a governmental function rather than a proprietary one. This is because such action,
22 purportedly required by state statute, would be more political, legislative, and performed for the
23 public good, as opposed to commercial or proprietary in nature.”); *Commerce Bank of Kansas City,*
24 *N.A. v. Housing Auth. of Kansas City, Mo.*, 62 F.3d 1123, 1125 (8th Cir. 1995) (noting funds in
25 pension plan assisting in performing “governmental function” because public agency “can only
26 function through its employees, and to hire and retain competent employees the [agency] reasonably
27 determined to provide a pension plan.”); *Currihan v. Stone*, 317 P.2d 1044, 1049 (Colo. 1959)
28 (“Creation of the Police Pension and Relief Fund, control and administration thereof by the City . . .
are all a part of and are inextricably interwoven into the creation and maintenance of the Police
Department of the City of Denver, and the exercise of control over the fund is a governmental
function.”); *Glassman v. Glassman*, 131 N.E.2d 721, 727 (N.Y. 1956) (“That the Retirement System
is an arm or agency of the State performing the public function of providing and regulating pensions
for public employees cannot be doubted.”); *Bd. of Trustees of Police Pension Fund of Glen Ellyn v.*
Village of Glen Ellyn, 85 N.E.2d 473, 481 (Ct. App. Ill. 1949) (“the duties imposed upon a
municipality with reference to the establishment of police pension funds are government in
character.”); *Ayers v. City of Tacoma*, 108 P.2d 348, 352 (Wash. 1940) (holding local “pension
system” is a “governmental function directed toward more effective public service, which is a benefit
to the city.”).

1 ii. *In Any Event, Section 20487 Is Not Preempted by the Bankruptcy Code.*

2 As discussed above with respect to the conclusion that the Bankruptcy Code does not
3 generally preempt the PERL, neither express nor field preemption apply so as to render section 20487
4 ineffective in chapter 9. The only remaining form of preemption which could apply so as to preempt
5 section 20487 is conflict preemption. Conflict preemption occurs only when (1) “compliance with
6 both federal and state regulations is a physical impossibility;” or (2) in “those instances where the
7 challenged state law stands as an obstacle to the accomplishment and execution of the full purposes
8 and objectives of Congress.” *Arizona v. United States*, 132 S. Ct. 2492, 2501 (2012) (quotations and
9 citations omitted); *see also In re Thorpe Insulation Co.*, 677 F.3d 869, 889 (9th Cir. 2012), *cert.*
10 *denied*, 133 S. Ct. 119 (2012). “Implied preemption analysis **does not** justify a ‘freewheeling judicial
11 inquiry into whether a state statute is in tension with federal objectives’; such an endeavor ‘would
12 undercut the principle that **it is Congress rather than the courts** that preempts state law.’” *Chamber*
13 *of Commerce of the U.S. v. Whiting*, 131 S. Ct. 1968, 1985 (2011) (emphasis added) (quoting *Gade v.*
14 *Nat’l Solid Wastes Mgmt. Ass’n.*, 505 U.S. 88, 111 (1992) (Kennedy, J., concurring)). “Our
15 precedents ‘establish that a high threshold must be met if state law is to be preempted for conflicting
16 with the purposes of a federal Act.’” *Id.* at 1985 (quoting *Gade*, 505 U.S. at 110)). Under binding
17 Supreme Court preemption precedents, section 20487 comes to this Court with a very strong
18 presumption in favor of its constitutionality.

19 (a) Physical Impossibility Preemption Does Not Apply.

20 Any claim that “physical impossibility” applies is easily dispatched. Section 365(a) provides
21 that a debtor “**may** assume or reject any executory contract.” 11 U.S.C. § 365(a) (emphasis added).
22 Thus, under 365(a) the choice to assume or reject rests within the discretion of the municipal debtor.
23 If it does neither, the contract “rides through” the bankruptcy. *See, e.g., Smith v. Hill*, 317 F.2d 539,
24 542 n.6 (9th Cir. 1963). However, section 20487 prohibits rejection and requires approval for
25 assumption. There is no “physical impossibility” between the two because under section 365(a), a
26 municipal debtor has the option of deciding what to do with its executory contracts. If the Code
27 required otherwise—that a debtor must reject such contracts—physical impossibility might have
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1 some role to play. Because it expressly does not, “physical impossibility” preemption does not exist
2 because a debtor can, like Stockton, comply with both federal and State law.

3 (b) Obstacle Preemption Does Not Apply.

4 The key to “obstacle” preemption, as noted, is whether the State law “stands as an obstacle to
5 the accomplishment and execution of the full purposes and objectives of Congress.” *Arizona*, 132 S.
6 Ct. at 2501 (quotations and citations omitted). Again, the “two cornerstones” of every preemption
7 analysis are (1) Congressional intent and (2) the presumption against preemption. *Wyeth v. Levine*,
8 555 U.S. 555, at (2009). In assessing Congress’s intent to preempt, courts must first focus on the
9 statutory language which, of course, “contains the best evidence of Congress’s pre-emptive intent.”
10 *CSX Transp., Inc. v. Easterwood*, 507 U.S. 658, 664 (1993); *CTS Corp. v. Waldburger*, 134 S. Ct.
11 2175, 2185 (2014) (“Congressional intent is discerned primarily from the statutory text.”).

12 Here, Congress gave no indication through the statutory text of section 365(a) into whether it
13 intended to preempt State laws protecting pension rights in chapter 9. Section 365(a) is completely
14 silent on that matter. Nor is CalPERS aware of any legislative history indicating whether section
15 365(a) was intended to displace State laws expressly precluding rejection of a debtor’s relationship
16 with its State-run pension system. Thus, it cannot be said that Congress expressed its intent in a “clear
17 and manifest” enough manner in section 365(a) to overcome the presumption against preemption that
18 applies to Cal. Gov. Code § 20487. *BFP v. Resolution Trust Corp.*, 511 U.S. 531, 544 (1994). The
19 administration and provision of public pensions is an area of traditional State regulation and exercise
20 of the historic police powers of the States. *See* CalPERS’ Supplemental PERL Brief, § II.A.1. As the
21 Supreme Court made clear, absent such a “clear and manifest” expression by Congress, “the
22 Bankruptcy Code will be construed to adopt, rather than displace, pre-existing state law.” *Id.* at 544-
23 45.

24 Likewise, given the relationship that exists between a municipal debtor and the laws of the
25 State of California, which has expressly forbidden contracting agencies to reject their relationship
26 with CalPERS, any such “liberating preemption would come only by interposing federal authority
27 between a State and its municipal subdivision]” *Nixon v. Missouri Muni. League*, 541 U.S. 125,
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1 140 (2004). Thus, the Supreme Court has instructed that courts apply a “working assumption that
2 federal legislation threatening to trench on the States’ arrangements for conducting their own
3 governments should be treated with *great skepticism*” *Id.* Applying the required “great
4 skepticism” leads to but one conclusion: that Congress did not intend to preempt laws like Cal. Gov.
5 Code § 20487 by means of section 365 of the Bankruptcy Code.

6 Reliance on the “broad remedial purposes” of the Code as a justification for preemption of
7 section 20487 would be inappropriate as the Supreme Court has rejected such purpose-driven
8 statutory construction. “After all, almost every statute might be described as remedial in the sense
9 that all statutes are designed to remedy some problem.” *CTS Corp.*, 134 S. Ct. at 2185. This is so
10 because “no legislation pursues its purposes at all costs.” *Rodriguez v. United States*, 480 U.S. 522,
11 525-26 (1987) (per curiam); *see also In re Transcon Lines*, 58 F.3d 1432, 1437-38 (9th Cir. 1995)
12 (“Invocation of the ‘plain purpose’ of legislation . . . takes no account of the processes of compromise
13 and, in the end, prevents the effectuation of congressional intent.”) (quoting *Bd. of Governors of the*
14 *Fed. Reserve Sys. v. Dimension Fin. Corp.*, 474 U.S. 361, 373-74 (1986)). In fact, the Supreme Court
15 has referred to the invocation of such “purposes” as the “last redoubt of losing causes” because
16 “[e]very statute proposes, not only to achieve certain ends, but also to achieve them by particular
17 means—and there is often a considerable legislative battle over what those means ought to be.” *Dir.*,
18 *Office of Workers’ Comp. Programs, Dep’t of Labor v. Newport News Shipbuilding & Dry Dock Co.*,
19 514 U.S. 122, 136 (1995).

20 The Supreme Court has recognized that the Bankruptcy Code does not reflect any such “broad
21 remedial purpose.” In rejecting similar reasoning, the Supreme Court concluded that “the Bankruptcy
22 Code . . . is not a remedial statute” in the sense that it is designed to protect and secure specific
23 interests. *Florida Dep’t of Revenue v. Piccadilly Cafeterias, Inc.*, 554 U.S. 33, 51 (2008); *see also*
24 *Schwab v. Reilly*, 560 U.S. 770, 791 (2010) (“none of Reilly’s policy arguments can overcome the
25 Code provisions” because such an “approach threatens to convert a fresh start into a free pass.”); *In*
26 *re Flores*, 735 F.3d 855, 861 (9th Cir. 2013) (en banc) (noting that the “fresh start” generality is “not
27 the end of the story”)); *In re Dumont*, 581 F.3d 1104, 1111 (9th Cir. 2009) (looking to the purposes
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1 of the Bankruptcy Code is not helpful because “Bankruptcy law serves two central but often
2 conflicting interests”); *Myers v. TooJay’s Mgmt. Corp.*, 640 F.3d 1278, 1286 (11th Cir. 2011).

3 Moreover, any claim that not allowing a City to reject its relationship with CalPERS might
4 make it more difficult to reorganize in some hypothetical sense is not supported by the actual facts of
5 this case. In any event, the Ninth Circuit has said “[s]imply making a reorganization more difficult
6 for a particular debtor . . . does not rise to the level of ‘standing as an obstacle to the accomplishment
7 of the full purposes and objectives of Congress.’” *In re Thorpe*, 677 F.3d at 890-91 ((quoting *In re*
8 *Baker & Drake, Inc.*, 35 F.3d 1348, 1354 (9th Cir. 1994) (quoting *Schneidewind v. ANR Pipeline Co.*,
9 485 U.S. 293, 300 (1988)).¹⁶ Thus, there is no evidence that, by not allowing the City to
10 hypothetically reject its relationship with CalPERS, section 20487 somehow stands as an obstacle to
11 the realization of Congress’s purposes in enacting chapter 9 and there is no basis to conclude that
12 section 20487 is preempted by the Bankruptcy Code.

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18 ¹⁶ Any suggestion that the Bankruptcy Code is the *only* means by which contracts may be impaired is
19 incorrect. In upholding a New Jersey law, the Supreme Court recognized that “a state insolvency act
20 is limited by the Contract Clause,” but such limitations depended “on what is affected by such
21 composition and what state power it brings into play. The dictum from *Sturges v. Crowninshield* [4
22 Wheat. 122 (1819)] is one of those ***inaccurate generalizations that has gained momentum from***
23 ***uncritical repetition.***” *Faitoute Iron & Steel Co. v. City of Asbury Park*, 316 U.S. 502, 513 (1942)
24 (emphasis added). Contracts may also be impaired under California law, notwithstanding California’s
25 Contracts Clause. *See, e.g., Sonoma Cnty. Org. of Pub. Emps v. Cnty of Sonoma*, 23 Cal. 3d 296, 305
26 (1976) (“Our inquiry, then, concerns not whether the state may in some cases impair the obligation of
27 contracts, but the circumstances under which such impairment is permissible”). Since *Faitoute*, the
28 Supreme Court has affirmed that the Contracts Clause should not be so broadly interpreted. *See*
Allied Structural Steel Co. v. Spannaus, 438 U.S. 234, 240 (1978) (stating that while the language of
the Contracts Clause appears absolute, “it is not . . . the Draconian provision that its words might
seem to imply”). Rather, State laws which impair contracts do not violate the clause so long as they
serve “a legitimate public purpose such as remedying a general social or economic problem,” and
“the means chosen to accomplish this purpose [are] reasonable and necessary.” *Buffalo Teachers*
Federation v. Tobe, 464 F.3d 362, 368 (2d Cir. 2006) (citing *Energy Reserves Group, Inc. v. Kansas*
Power & Light Co., 459 U.S. 400, 41-13 (1983)). Furthermore, the “Contracts Clause has been
construed narrowly in order to ensure that local governments retain the flexibility to exercise their
police powers effectively.” *Ching Young v. City & Cnty. of Honolulu*, 639 F.3d 907, 913 (9th Cir.
2011) (quotations omitted).

1 **D. *Mission Independent* Has No Application In this Case.**

2 Franklin's past reliance on the enigmatic dictum in *Mission Independent School District v.*
3 *Texas*, 116 F.2d 175 (1940), is misplaced. Franklin's Reply Regarding Pension Liabilities, p. 5 [Dkt.
4 No. 1397]. In that case, the court made an alternate, albeit dispositive, ruling on the question of
5 whether a 1939 law violated the Texas Constitution's prohibition against "deceptive and misleading"
6 titles to legislative acts. *Id.* at 178. On that ground alone, the court could have ordered the remand (to
7 confirm the plan) that it did, without addressing any of the federal constitutional issues, because the
8 1939 law did not repeal a 1935 law that authorized Texas's subdivisions to file for bankruptcy. *See*
9 *id.* at 177. Under settled principles of judicial restraint at that time, this would have been the correct
10 way to resolve this case. *See, e.g., Siler v. Louisville & Nashville R. Co.*, 213 U.S. 175, 193 (1909).
11 At best, the portion of *Mission Independent* on which Franklin and certain courts rely is dictum,
12 which has no precedential value. *See, e.g., Boykin v. Boeing Co.*, 128 F.3d 1279, 1282 (9th Cir. 1997)
13 ("Because this is dictum, we accord it no precedential value.").

14 In any event, *Mission Independent* is distinguishable or just plain wrong under modern day
15 jurisprudence. *First*, unlike today, the municipal bankruptcy law in effect at that time ***did not*** contain
16 any requirement that a municipality actually have any State authorization, let alone the "specific
17 authorization" now mandated by section 109(c)(2). *United States v. Bekins*, 304 U.S. 27, 49 (1938).
18 The decision is therefore contrary to the current chapter 9 because the legislative history of currently
19 applicable chapter 9 makes it clear that "withdrawal of State consent ***at any time*** will terminate the
20 case" H.R. REP. NO. 94-686, at 8, *reprinted in* 1976 U.S.C.C.A.N. 539, 545 (emphasis added).

21 *Second*, the Fifth Circuit did not construe the 1939 law as a bankruptcy authorization statute;
22 rather, it interpreted the law as excluding "bonds so owned [by the permanent school fund of Texas]
23 ***from the operation*** of any composition made." 116 F.2d at 177 (emphasis added). In its view, this
24 reading was the most "natural meaning" of the law in question. *See id.* Thus, in the Fifth Circuit's
25 view, Texas sought to exempt its own bonds from treatment in bankruptcy independently of its
26 authorization to be in bankruptcy. In fact, at the time *Mission Independent* was decided, Texas had
27 two authorization laws on the books. *See id.* Thus, the case says nothing about whether or not a State
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1 can or cannot attach conditions in an authorization statute. States obviously can do so given that the
2 control they have over their municipal creatures is absolute. In contrast, the district court in that case
3 construed the law in question as an authorization statute and determined that the bankruptcy case
4 must be dismissed for lack of state authority to file. *See In re Mission Independent School Dist.*, 35 F.
5 Supp. 37, 39 (S.D. Tex. 1940). Had the Fifth Circuit read the statute as a bankruptcy authorizing
6 statute—which, as explained above, is how the California courts would construe section 20487—the
7 result would have been dismissal of the bankruptcy case.

8 *Third*, and perhaps most importantly from a factual standpoint, the Fifth Circuit said:

9 The State of Texas ***bought the bonds it holds for the school fund, and paid for them***
10 ***just as others did***. It obtained no better right to repayment. The bonds it holds against
11 its own subdivisions ***as an investment*** stand just as though they were municipal bonds
12 issued in another state. The State of Texas is simply a bond creditor as others are.

13 116 F.2d at 178 (emphasis added). In sharp contrast, CalPERS is not appearing in this case as a
14 holder of Stockton bonds. Nor does California, through CalPERS, hold the money in the PERF as an
15 investment to fill the State's coffers with funds that the State is then free to spend. The exact opposite
16 is true. The funds California holds, through CalPERS, are trust funds and they can only be used to
17 pay out pension benefits and to administer the State-run system. *See* Cal. Gov. Code § 20170; *see*
18 *also* CAL. CONST., art. XVI, § 17(a). The funds held in the PERF stand on much different footing than
19 the bonds that Texas bought as an investment because their purpose is not to enrich the State treasury
20 or to help pay for the educational needs of California's citizens, but to instead fulfill a core
21 governmental objective in sustaining a viable public employee retirement system.

22 *Fourth*, nothing in the *Mission Independent* case mentions former section 83(i) of Chapter 10,
23 which largely mirrors section 903. As a result, the decision has absolutely nothing to say about what
24 section 903 does or does not mean. The decision is neutral on the matter. Moreover, it was only
25 because the court ruled the 1939 law unconstitutional under ***Texas law*** (but left in place the 1935
26 authorization statute), that it was able to avoid having to wrestle with the question of whether the
27 proposed plan, which it ordered to be confirmed, was consistent with State law as was required by
28 *Bekins* and the Federal act in effect at that time. Thus, *Mission Independent* does not address whether
section 943(b)(4) would prohibit a plan of adjustment that was inconsistent with State law.

1 *Finally*, the *Mission Independent* court’s 30,000 foot approach to preemption is not the law
2 today. For example, the court never discussed Congress’s intent nor did it even discuss any
3 presumption against preemption, let alone the heightened one that exists if a court is intruding into
4 the relationship between a State and one of its municipalities. *Nixon*, 541 U.S. at 140. Rather, by
5 simple *ipse dixit*, it declared that bankruptcy law reigned supreme. Such an approach is incompatible
6 with the modern-day Supreme Court’s preemption analysis. Had the court employed the required
7 “working assumption that federal legislation threatening to trench on the States’ arrangement for
8 conducting their own governments should be treated with great skepticism,” *id.*, the Fifth Circuit
9 would have been compelled to come to a contrary result.

10 **E. Congress’s Attempt to Abrogate State Sovereign Immunity Pursuant to 11 U.S.C. §**
11 **106(a) is Inapposite in This Case.**

12 During the July 8, 2014 hearing, this Court suggested that 11 U.S.C. § 106(a) had some role
13 to play in this Court’s analysis, saying:

14 And another item that is listed in Section 106(a)(1) is Section 944. Of course, 944 is
15 the effect of confirmation and includes the discharge, and the conventional analysis is
16 that the State of California by authorizing filing the Chapter 9 invokes Section 106 on
itself. And then, of course, the City of Stockton, to the extent it can avail itself of
sovereign immunity, invoked Section 106 on itself when it filed this case.

17 Hr’g Tr. 44-45, July 8, 2014. In fact, Franklin goes so far as to claim that “California has waived
18 whatever sovereignty protections CalPERS otherwise might possess by authorizing its municipalities
19 to file for bankruptcy.” Franklin’s Reply Regarding Pension Liabilities, p. 8 (citing *Stockton II*’s
20 citation to § 106(a)). In making this claim, Franklin misses the basic constitutional distinction
21 between State sovereignty and sovereign immunity.

22 As the Second Circuit explained:

23 While both Amendments protect the States, they deal with different aspects of state
24 sovereignty. The Tenth Amendment protects states from intrusion by the federal
25 government. It addresses state sovereignty generally and limits Congress’ exercise of
power pursuant to Article I. . . .

26 The Eleventh Amendment protects States from suits by its citizens in federal court. It
27 is concerned with judicial authority and limits the power of Article III courts over
actions brought against States.

1 *Close v. State of New York*, 125 F.3d 31, 39 (2d Cir. 1997). In *Printz*, the Supreme Court made this
2 exact point by noting that the Tenth Amendment’s federalism protections are broader than the
3 Eleventh Amendment’s immunity from suit. *Printz v. United States*, 521 U.S. 898, 931 n.15 (1997).
4 The former protects the States and their municipalities, while the latter protects only the States. It is
5 for this reason that States and their arms have sovereign immunity, while municipalities do not. *See*,
6 *e.g.*, *Jinks v. Richland Cnty., S.C.*, 538 U.S. 456, 466 (2003) (“[M]unicipalities, unlike States, do not
7 enjoy a constitutional immunity from suit.”); *Alden v. Maine*, 527 U.S. 706, 756 (1999) (“The
8 immunity does not extend to suits prosecuted against a municipal corporation or other governmental
9 entity which is not an arm of the State.”); *Monell v. Dep’t of Social Servs. of City of New York*, 436
10 U.S. 658, 691 n.54 (“Our holding today is, of course, limited to local government units which are not
11 considered part of the State for Eleventh Amendment purposes.”).¹⁷

12 As explained above, while a State may waive its sovereign immunity, it may not waive the
13 protections of federalism because the protections, unlike sovereign immunity, do not belong to the
14 States alone. *See supra* § III.A.2 (discussing the Supreme Court’s *Bond I* and *New York* decisions).
15 Putting this question aside, even on its own terms, Franklin’s argument is incorrect.

16 The “test for determining whether a State has waived its immunity from federal-court
17 jurisdiction is a stringent one. A State’s consent to suit must be unequivocally expressed *in the text of*
18 *the relevant statute* [and] [w]aiver may not be implied.” *Sossaman v. Texas*, 131 S. Ct. 1651, 1658
19 (2011) (quotations and citations omitted) (emphasis added). “There can be no consent by implication
20 or by use of ambiguous language. Courts must indulge every reasonable presumption against waiver .
21 . . .” *Holley v. Cal. Dep’t of Corrections*, 599 F.3d 1108, 1111-12 (9th Cir. 2010) (quotations,
22 alteration & citation omitted). Franklin’s suggestion that California waived its sovereign immunity,
23 or any aspect of its sovereignty, by merely authorizing its creatures to file for chapter 9 is wrong as a
24 matter of constitutional law.

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27 ¹⁷ Under these cases, the Court’s comment that the City invoked 106(a) on itself by filing this case is
28 incorrect. Section 106(a) has no role to play with respect to the City because Congress did not need to
attempt to abrogate the City’s sovereign immunity because the City does not enjoy such immunity.

1 Nothing in the language of the Municipal Bankruptcy Authorization Statute expressly or
2 unequivocally states that California waived anything, including its immunity from suit. Indeed, the
3 opposite is true. Cal. Gov. Code § 53760.7 states, in pertinent part:

4 No cause of action against the state, or any department, agency, entity of the state, or
5 any officer or employee of the state acting in their official capacity may be maintained
6 for any activity authorized by this article, or for the act of a local public entity filing
under Chapter 9 of Title 11 of the United States Code, including any proceeding
following a local public entity's filing.

7 Thus, under the authorization statute, California expressly sought to retain its immunity from being
8 haled into federal court against its will by one of its subdivisions. And by extension, even if
9 California could waive its sovereignty, as Franklin claims, nothing in the authorization statute does
10 that. As a result, California waived nothing by generally authorizing its municipalities to file for
11 chapter 9.

12 Nothing in section 106(a) supports a contrary result. Section 106(a) states: "Notwithstanding
13 an assertion of sovereign immunity, sovereign immunity is abrogated as to a governmental unit to the
14 extent set forth in this section" In enacting the Bankruptcy Reform Act of 1994, Congress
15 sought, through section 106(a), to "overrule two Supreme Court cases that have held that the States
16 and Federal Government are not deemed to have waived their sovereign immunity by virtue of
17 [Congress] enacting section 106(c) of the Bankruptcy Code." H.R. Rep. No. 103-835, at *42 (1994),
18 *reprinted in* 1994 U.S.C.C.A.N. 3340, 3342 (discussing *Hoffman v. Connecticut Dep't of Income*
19 *Maint.*, 492 U.S. 96 (1989) & *United States v. Nordic Village, Inc.*, 503 U.S. 30 (1992)). For
20 example, in *Hoffman*, the Supreme Court held, in enacting former section 106(c), which contained
21 the phrase "notwithstanding any assertion of sovereign immunity," that Congress did not make its
22 intention to abrogate State sovereign immunity with respect "to over 100 Code provisions"
23 unmistakably clear. 492 U.S. at 101-04 (plurality). As such, former 106(c) was insufficient to
24 constitute a valid abrogation of State sovereign immunity. In his concurrence, Justice Scalia (who on
25 this point was joined by Justice O'Connor) went even further and concluded that under the
26 Bankruptcy Clause Congress lacked the power to abrogate State sovereign immunity. 492 U.S. at 105
27 (Scalia, J., concurring in the judgment).

1 In *Seminole Tribe of Florida v. Florida*, 517 U.S. 44 (1996), the Supreme Court adopted
2 Justice Scalia’s position and held that, while Congress had the authority to abrogate State sovereign
3 immunity under Section 5 of the Fourteenth Amendment, it could not do so under its Article I
4 powers. 517 U.S. 44, 72-73 (1996) (“The Eleventh Amendment restricts the judicial power under
5 Article III, and Article I cannot be used to circumvent the constitutional limitations placed upon
6 federal jurisdiction.”). The Court reaffirmed this principle several times. *Bd. of Trustees of Univ. of*
7 *Alabama v. Garrett*, 531 U.S. 356, 364 (2001); *Kimel v. Florida Bd. of Regents*, 528 U.S. 62, 79
8 (2000); *Florida Prepaid Postsecondary Educ. Expense Bd. v. Coll. Sav. Bank*, 527 U.S. 627, 628
9 (1999).

10 Based on these precedents, the Ninth Circuit held that, although section 106(a) was
11 sufficiently clear to demonstrate Congress’s intent to abrogate State sovereign immunity, this did not
12 matter because Congress lacked the constitutional authority to abrogate State sovereign immunity
13 under the Bankruptcy Clause. *In re Mitchell*, 209 F.3d 1111, 1121 (9th Cir. 2000) (“Thus, we
14 conclude that Congress did not act within the scope of its abrogation power in enacting § 106(a).”).
15 In other words, section 106(a)’s purported abrogation of sovereign immunity is ineffective and
16 unconstitutional. *Accord In re Death Row Records, Inc.*, 2012 WL 952292, at *5 (9th Cir. BAP Mar.
17 21, 2012).

18 Here, the question of whether pensions can be impaired does not turn on whether or not
19 Congress validly abrogated State sovereign immunity in section 106(a). Under *Mitchell*, we know
20 that it has not. After all, sovereign immunity is an immunity from suit and nothing more. Thus,
21 whether or not California or CalPERS waived its sovereign immunity is beside the point.

22 Franklin’s suggestion that the Supreme Court’s decisions in *Van Huffel v. Harklerode*, 284
23 U.S. 225 (1931), and *New York v. Irving Trust Co.*, 288 U.S. 329 (1933), which both predate chapter
24 9, stand for the broad proposition that pensions can be impaired completely misses the mark.
25 Franklin’s Reply Regarding Pension Liabilities, p. 8.¹⁸ Neither case involved a municipal debtor. As
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27 ¹⁸ Likewise, the Supreme Court’s decision in *Gardner v. New Jersey*, 329 U.S. 565 (1947) has no
28 application here because that case merely stands for the proposition that, if a State files a proof of
claim, it waives its sovereign immunity. *See, e.g., In re Pegasus Gold Corp.*, 394 F.3d 1189, 1195-96

1 the district court in San Bernardino recently noted, this alone changes the analysis, given the
2 relationship that exists between a State and one of its subdivisions. *In re City of San Bernardino*,
3 2014 WL 2511096, at *12 (C.D. Cal. June 4, 2014) (“Municipal bankruptcies implicate a state’s
4 sovereignty and Tenth Amendment rights to a greater degree than other bankruptcy contexts because
5 of the special relationship between a state and its municipalities.”). Also, neither case says anything
6 about the Tenth Amendment, but only address general questions regarding the treatment of States in
7 bankruptcy proceedings. For example, *Irving Trust* addresses only the question of whether a State is
8 bound by a discharge order whether or not they participate in the bankruptcy. *Irving Trust*, 288 U.S.
9 at 333. Neither of those cases address, even remotely, the substance of any of the issues that might be
10 before this Court with respect to the power to impair or adjust pensions.

11 At the end of the day, while the intersection of bankruptcy and State sovereign immunity
12 presents complex questions, the question of sovereign immunity is inapposite to the resolution of this
13 case and the question of whether a chapter 9 plan of adjustment can impair or adjust pension
14 obligations.

15 III. CONCLUSION

16 To the extent the Court addresses any of these issues, constitutional principles of sovereignty
17 embodied in the Tenth Amendment to the Constitution, section 903 of the Bankruptcy Code, and
18 State law, including the PERL, all must be given meaning, leading to the inescapable conclusion that
19 a municipality may not impair or adjust its statutory obligations to CalPERS through a chapter 9 plan
20 of adjustment and may not reject its relationship with CalPERS pursuant to section 365 of the
21 Bankruptcy Code.

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24 (9th Cir. 2005). CalPERS has not filed a proof of claim in this case, so *Gardner* cannot form the basis
25 for any claim of waiver. Indeed, 11 U.S.C. § 106(b) merely codifies *Gardner*. *In re Jackson*, 184 F.3d
26 1046, 1049 (9th Cir. 1999). Similarly, the Court’s decision in *Tennessee Student Assistance Corp. v.*
27 *Hood*, 541 U.S. 440 (2004), does not apply. There, the Court determined that a bankruptcy court’s
28 exercise of its *in rem* jurisdiction in deciding an adversary proceeding relating to an undue hardship
finding was not a “suit” for purposes of the Eleventh Amendment. *Id.* at 451 (“We thus hold that the
undue hardship determination sought by Hood in this case is not a suit against a State for purposes of
the Eleventh Amendment.”).

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Respectfully submitted,

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