



NUVEEN ASSET MANAGEMENT

States Cannot Declare Bankruptcy

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States cannot declare bankruptcy

With comments swirling in the latest news cycle suggesting the idea of states declaring bankruptcy, our municipal investment team provides some perspective. In short, states cannot declare bankruptcy and state budget challenges do not mean insolvency.

Insights from

Nuveen's Municipal Investment Team

STATES CANNOT DECLARE BANKRUPTCY

- No state is talking about declaring bankruptcy.
- States themselves do not have access to bankruptcy due to prohibitions in the U.S. Constitution. Individual states can allow their underlying governments and instrumentalities access to bankruptcy and set certain state-specific eligibility requirements.
- The U.S. Supreme Court found Chapter 9 unconstitutional in 1936 for impeding states' rights, because the court found that sovereign states cannot submit to the federal government. Bankruptcy would violate the sovereignty of states set forth in the Constitution, where a judge and Congress could then hold sway over a state's fiscal affairs.

- Allowing states to file for bankruptcy was raised during the last recession. It drew widespread disdain, as it would unsettle the bond market and cause even fiscally sound states to face higher interest rates due to the risk the debt could be wiped out in court.

STATE BUDGET CHALLENGES DO NOT MEAN INSOLVENCY

- Many states are facing budget deficits, unfunded pension liabilities and high fixed costs, but these challenges should not be equated with insolvency.
- States have broad powers to control their own taxation and spending, and may have access to rainy day funds. In many cases, the solutions to states' fiscal and budgetary challenges are political, best solved by new policy decisions.
- Pensions are long-term liabilities, so no state is likely to face any kind of near-term solvency issue due to pension liabilities.

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- Less aid and support from the federal government means states may have to impose austerity measures to balance their budgets. That could lead to more state employees joining the ranks of the unemployed, higher tax rates, further neglect of critical public infrastructure improvements and continued stress on pension liabilities.
- Many state governments are projecting significant revenue declines and budget deficits

due to the decline in economic activity. Although some states have provided early estimates, the magnitude of these budget deficits is difficult to predict with certainty, given the unknown duration of the shutdown.

LEARN MORE

Please refer to our [paper on municipal bankruptcies](#) for additional insights.

For more information, please contact visit us at nuveen.com.

Endnotes

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