

Dan Walters: Stockton case may hit pension status

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Ever since Stockton filed for bankruptcy two years ago, Judge Christopher Klein has strongly hinted that he's willing — perhaps even eager — to declare that city employee pension obligations are debts that could be trimmed along with those of more conventional creditors.

"We have a festering sore here," Klein said earlier this year. "We got to get in there and excise it and figure out what the story is."

Klein's obvious leanings have drawn strenuous objections from the California Public Employees Retirement System (CalPERS). It has advanced several legal theories as to why pensions should be exempted from the haircuts other creditors are taking.

At first, it relied on a section of the state constitution prohibiting the impairment of contracts, but Klein undermined that theory when he reminded attorneys, "bankruptcy is nothing but the impairment of contracts."

When Detroit filed for bankruptcy, the judge in its case flatly declared that pension obligations would be treated like other debts and could be modified. But CalPERS insisted that California was different because it is a state agency and therefore has sovereign immunity.

Last week, however, Klein more or less dismissed that argument as he indicated again that he's inclined to declare pensions to be fair game in bankruptcy proceedings.

The real creditors on pensions are the current and potential city retirees while CalPERS "is in effect a servicing agency," Klein said.

San Bernardino, after initially saying it wanted to reduce pension debts in its bankruptcy and incurring CalPERS' wrath, has shifted and has a recovery plan that doesn't include pension cuts.

Stockton has never wanted to touch pensions but one of its creditors — the only one without a settlement deal — claims that ignoring pension debts is unfair to other creditors.

Klein said last week that even if Stockton makes deals with all its creditors, he may still declare pension debts to be at risk, implying that he wants appellate courts to end the uncertainty.

He invited parties in the bankruptcy case to "straighten me out before I make some dramatic boneheaded mistake" about the status of pensions, but left no doubt that he was leaning in that direction.

Klein's remarks provide a pathway to settling the issue without visiting more pain on Stockton's current and future pensioners, who already have seen cutbacks in their health care.

If all creditors agree, Stockton's bankruptcy could end amicably, but with a pension ruling that CalPERS would certainly take to the appellate courts to prevent its being an immediate precedent.

Coupled with what happened in Detroit, that process would result in a definitive ruling so that local governments everywhere and their creditors would know the risks of insolvency, rather than fighting them out case by case.

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