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Preserving Local Autonomy in the Face of Municipal Financial Crisis: Reconciling Rhode Island’s Response to the Central Falls Financial Crisis with the State’s Home Rule Tradition

Katherine Newby Kishfy*

INTRODUCTION

A. Municipal Insolvency: Central Falls’ Financial Crisis and a Rapid State Response

On May 19, 2010, the “City with a Bright Future,” but many financial problems, achieved a Rhode Island first: with the approval of the City Council, the City’s Mayor petitioned the Rhode Island Superior Court for judicial receivership claiming that the City was insolvent.1 The Superior Court Justice acquiesced to the distressed municipality’s request and appointed a temporary receiver for the City, who, it was hoped, would be able to relieve some of the strain on the City’s coffers by

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1. See John Hill, City in Receivership, PROVIDENCE J., May 20, 2010, at A1 [hereinafter City in Receivership]. Although other Rhode Island municipalities, as well as Central Falls itself, have previously faced extreme financial strain, none has actually petitioned for bankruptcy or receivership. Id.
negotiating new, more favorable contract terms, particularly with regard to municipal employees. At the time, Central Falls was facing an "extraordinary" financial emergency – the City projected a budget shortfall of $3,000,000 for the 2010 fiscal year and $5,000,000 in 2011. Additionally, the City had municipal bond indebtedness of $10,000,000 and accrued pension liability exceeding $35,000,000, but no funds to satisfy over $1,500,000 in pension fund obligations due during the 2010 fiscal year. Looking down the barrel of "extreme fiscal stress," the City Council passed a Resolution allowing the Mayor to file a receivership petition. Central Falls' capital market rating was immediately downgraded to junk bond status, and state officials were informed that as a result of the judicial receivership, "capital markets would view debt financing to Rhode Island municipalities as extremely risky and it would become more expensive for municipalities to borrow in the capital markets."

State officials, who were apparently uninvolved in the decision to file for receivership, immediately set the gears in

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2. See id.
3. See Pfeiffer v. Moreau, C.A. No. PB 10-5615, slip op. at 6 (R.I. Super. Ct. Oct. 18, 2010), available at http://www.courts.state.ri.us/superior/pdf/10-5615.pdf. Financial strife is not a new phenomenon in Central Falls. In fact, in 1991 when the city faced a similar financial crises, the Rhode Island General Assembly passed an act entitled "Central Falls – Fiscal Emergency Act" after determining that "the public health and welfare of the citizens of Central Falls and of this state would be adversely affected by the insolvency of the local government of Central Falls," such that state intervention was necessary to "protect the credit of the state and its political subdivisions." R.I. GEN. LAWS § 45-52.1-1 (repealed 2005). In that instance, the General Assembly implemented a financial review commission comprised of a variety of state and local stakeholders to assist the city in identifying and implementing measures that would lead to a balanced budget. R.I. GEN. LAWS § 45-52.1-3 (repealed 2005).
5. Id. at 7.
6. Black's Law Dictionary defines a junk bond as "[a] high-risk, high-yield subordinated bond issued by a company with a credit rating below investment grade." BLACK'S LAW DICTIONARY 204 (9th ed. 2009). Junk bonds are generally considered to be risky investments because they are heavily subordinated and, as such, they often carry higher-than-normal interest rates.
motion to regain control of the situation. Even though then-existing Rhode Island law provided for a financial oversight mechanism whereby the state's director of revenue could install a Budget and Review Commission to oversee municipal finances, the triggering conditions had apparently not yet been met. Rhode Island's Governor publicly voiced his concerns about the effect that the receivership could have on other municipalities and on the state as a whole, while others in the state government feared that Central Falls' receivership petition could "trigger a domino effect" of additional receivership petitions among other struggling Rhode Island cities and towns. The General Assembly sprang into action, hoping to remove Central Falls from receivership, passing "An Act Relating to Cities and Towns - Providing Financial Stability," that would apply retroactively to be effective as of several days prior to Central Falls' receivership petition. The day after the Governor signed the bill into law, the state's director of revenue exercised her new powers under the statute, appointing a permanent non-judicial Receiver for the city. In response, the Central Falls Mayor and City Council withdrew their motion for the appointment of a permanent judicial Receiver and began the transition to a non-judicial receivership provided for by the new legislation.

All was not well on the public opinion front, however. An
editorial published by The Providence Journal in the days following Central Falls’ initial receivership petition expressed dismay with the City’s elected officials, lamenting that “[n]ow, power has been taken away from them – and the voters – and given to an unelected receiver.”\(^{14}\) Several weeks after the City entered receivership, Rhode Island’s chapter of the American Civil Liberties Union raised questions as to the constitutionality of the new legislation under the Home Rule provision in the state’s constitution.\(^{15}\)

Against this backdrop, tensions escalated between the recently elected Mayor and City Council on one side, and the state-appointed Receiver on the other, after the Receiver requested that the Mayor relinquish his City vehicle and his keys to city hall, reduced his salary, and informed him that his role moving forward would be purely advisory.\(^{16}\) The power struggle between the two culminated in a courtroom showdown after both the Mayor and the Receiver attempted to appoint different individuals to the Central Falls Housing Authority Board.\(^{17}\) The Receiver filed suit seeking a determination from the court that the new legislation was constitutional and injunctive relief against both the Mayor and members of the City Council, who he claimed were interfering with his official actions as Receiver.\(^{18}\) Within days, the Mayor and City Council members countered with their own suit, challenging the constitutionality of the legislation on sundry grounds and seeking to restrain the Receiver from further action in his capacity under the statute.\(^{19}\) The two suits were consolidated, and the hearing justice found for the Receiver, rejecting arguments that the Act was unconstitutional, and finding that the Receiver had acted within the scope of his authority.\(^{20}\) The Mayor and City Council members took an appeal on the constitutional issues, and the case is currently pending.


\(^{16}\) See Pfeiffer, C.A. No. PB 10-5614, at 4 & n.3.

\(^{17}\) See id. at 4-5.

\(^{18}\) See id. at 5.

\(^{19}\) See id. at 5-6.

\(^{20}\) *Id.* at 47-48.
before the Rhode Island Supreme Court.\(^2\)

This Comment will compare Rhode Island's new municipal insolvency statute to the state's previous budget commission provision, both with reference to the pending constitutionality issue as well as its strengths and weaknesses as an economic policy, and will argue that although the statute is likely constitutional and incorporates an appropriate level of local participation on its face, as implemented in Central Falls' case, it does not comport with the democratic ideals embodied in Rhode Island's Home Rule provision. Furthermore, because the Act severely limits local participation in the budgetary reform process, it hinders long-term economic improvement in Central Falls. Part I of this Comment will explore the various legal mechanisms that have developed over time to resolve municipal financial crises, the nexus between opportunities for local input and lasting budgetary reform, and the legal framework under which Rhode Island's Home Rule Amendment, the primary guarantor of local governance, has been interpreted by the Rhode Island Supreme Court. Part II will analyze the new statute, its constitutionality under the Home Rule Amendment, and the practical implications of its policies and structure. Part III will offer policy recommendations for responding to municipal financial crises in a manner that maximizes the opportunity for local input, and comports with the democratic values underlying Rhode Island's Home Rule guarantee. Finally, Part IV will provide concluding remarks.

I. BACKGROUND

A. Snapshot of Municipal Insolvency – A Historical Framework

Prior to the Great Depression, neither the federal government nor most states had enacted general legislation to deal with municipal insolvency or bankruptcy in any uniform fashion.\(^2\)
Instead, municipal insolvency issues were generally governed by state and federal common law. Although cities frequently defaulted on debt obligations even prior to the widespread financial crisis of the Great Depression, there was no standardized bankruptcy code providing creditors' remedies, and instead creditors relied on judicially crafted remedies such as seizure of municipal or resident owned property, garnishment of city tax revenue, judicial imposition of new taxes, and judicial oversight of expenditures to prevent diversion from debt obligations. One key issue in these early cases was whether the same level of judicial oversight that was typical in private bankruptcy contexts extended to the municipal insolvency setting as well. For example, while bankruptcy provisions for private entities allowed court supervision over the day-to-day affairs and expenditures of a debtor, the Supreme Court had established that with respect to public entities, "the question [of] what expenditures are proper and necessary for the municipal administration, is not judicial; it is confided by law to the discretion of the municipal authorities. No court has the right to control that discretion." Thus, even in

Clause prevented states from enacting legislation that would readjust municipal debt, and principles of state autonomy embodied in the Tenth Amendment prevented the federal government from doing so as well. See id. at 427-28. In fact, the Supreme Court struck down Congress's first attempt at a federal municipal bankruptcy provision because it impermissibly intruded on state sovereignty. Ashton v. Cameron Cnty. Dist., 298 U.S. 513, 531 (1936).

24. Id. Although many of these remedies were analogous to traditional creditor's remedies against private entities, in the municipal context they were applied in a modified manner. Id. For example, in the private setting, creditors could seize debtor property for the purpose of satisfying obligations, but with municipal debtors, the Public Trust Doctrine typically prevented courts from permitting the seizure of property that was held for the public good. Id. at 430-31; see, e.g., Town of Farmerville v. Commercial Credit Co., 136 So. 82, 85 (La. 1931) (noting that "an execution cannot be levied on any property held by a municipality or other public corporation for public purposes, . . . the principle being that title to such property is held in trust for the public.") (citation omitted).
26. East St. Louis v. Zebley, 110 U.S. 321, 324 (1884). Similarly, in rejecting a creditor's attempt to enforce a debt against a city, the Court of Appeal of Louisiana noted that "the framing of their budgets seems to be a matter which is left to the discretion of the town councils, and courts are without authority to regulate them in preparing or supplementing the same."
the context of pre-statutory mechanisms for addressing with municipal insolvency, issues of municipal sovereignty were at the forefront of the debate, and the judiciary demonstrated a reluctance to invade the traditionally political areas of municipal taxing and spending, holding instead that absent statutory authority to appoint a receiver, it was inappropriate for a court to assert control over municipal operations analogous to that which a court could exert over a private debtor.27

Eventually, a handful of states responded to this uncertainty by providing statutorily for municipal receivers or financial oversight boards that had the authority to make changes to taxing and expenditures within the municipality.28 New England states took a particularly novel approach, enforcing municipal debt directly against residents based on the rationale that because

[t]owns, parishes, [and] precincts . . . [ ] are but a collection of individuals with certain corporate powers for political and civil purposes, without any corporate fund from which a judgment can be satisfied . . . each member of the community is liable in his person or estate to the execution which may issue against the body.29

In some instances, states took responsibility for municipal debt under the theory that cities and towns are but creatures of the state, "[b]ut it was never thought that states had a legal obligation

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27. See McConnell & Picker, supra note 22, at 436.

28. Id. For example, when Memphis became plagued by creditors' suits as a result of the city's chronic inability to collect taxes, Tennessee passed an act abolishing the City of Memphis as a municipal corporation, instead incorporating city property, assets, and residents into the body of the state, and appointing a receiver to manage tax collection and expenditures. Meriwether v. Garrett, 102 U.S. 472, 502-04, 508 (1880). Subsequently, in a consolidated suit brought by a variety of Memphis's creditors, a federal court appointed its own receiver to manage tax collection, payment of debt, and municipal expenditure, those greatly in excess of powers previously vested with any such judicial officer. Id. at 508. While the Supreme Court affirmed the authority of the state to repeal the charter of the municipality and appoint a receiver, reasoning that that the municipality is a "mere instrumentalit[y] of the State for the more convenient administration of local government," the Court held that in appointing its own receiver, the federal judge impermissibly encroached upon the prerogative of the state legislature. Id. at 511, 521.

29. See Meriwether, 102 U.S. at 519; Merchants Bank v. Cook, 21 Mass. 405, 414 (1826); McConnell & Picker, supra note 22, at 437.
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...to do these things, or that states stood behind the debts of their cities.”

However, in response to an ever-increasing need for a uniform approach during the Great Depression, as well as the holdout problem that developed when creditors were permitted to proceed individually rather than as a group, in 1937 Congress enacted what was intended to be a temporary emergency measure providing a federal municipal bankruptcy mechanism. By 1946, the provision was made permanent, eventually evolving into Chapter 9 of the Federal Bankruptcy Code, and is currently one of several debt restructuring devices available to insolvent municipalities. In recent years, several large cities have faced financial crises that have prompted either bankruptcy filing or some other form of state intervention. In addition to the highly publicized insolvencies of several major American cities, twenty-

31. During the run up to the Great Depression, the value of property increased rapidly, leading to increased property tax revenue, and prompting municipalities to expand municipal services and obtain long-term loans to finance infrastructure improvements. Omer Kimhi, Chapter 9 of the Bankruptcy Code: A Solution in Search of a Problem, 27 YALE J. ON REG. 351, 362 (2010) [hereinafter Chapter 9 of the Bankruptcy Code]. However, when the stock market later crashed and the real estate values plummeted, municipalities found themselves unable to cover municipal debts and obligations. Id. at 362-63.
32. McConnell & Picker, supra note 22, at 428. One of the bill’s supporters described the holdout problem that occurred when municipal creditors jockeyed to position themselves favorably: “[i]n every instance where a governmental unit finds itself in financial difficulty and is able to make some satisfactory agreement of adjustment with the majority of its creditors, there is always a small minority who hold out and demand preferential treatment.” Id. at 450 (quoting Hearing on HR 1670, HR 3083, HR 4311, HR 5009, and HR 5267 Before the H. Comm. on the Judiciary, 73d Cong., 1st Sess. 86 (1933) (statement of Rep. J. Mark Wilcox)). Therefore, to the extent that a collective process can be forced upon creditors, a holdout will not receive a disproportionate benefit as a reward for his failure to go along with the group. Id.
33. Id. at 428, 450, 454.
six states have reported that at least one municipality has experienced financial crisis in recent years.\textsuperscript{35}

B. A Catalog of Responses – Current Approaches to Municipal Insolvency

Today, there are three primary approaches to dealing with creditors' claims in the face of municipal insolvency.\textsuperscript{36} The first is through the traditional creditors remedies, similar to those that were utilized prior to Congressional enactment of the municipal bankruptcy code, which have analogs in private debt contexts.\textsuperscript{37} As noted above, many of the traditional remedies are often of little use to municipal creditors because while a creditor of a private entity may be able to seize an asset for sale, legislatures and many courts have precluded creditors from similarly seizing municipal property and financial assets.\textsuperscript{38} However, some courts have been willing to issue writs of mandamus, compelling a municipality to levy taxes in order to satisfy specific debts, and forcing the municipality's residents to indirectly foot the bill for the debt.\textsuperscript{39}

The second avenue for creditor recovery is provided for by the Chapter 9 of the Federal Bankruptcy Code.\textsuperscript{40} Importantly, municipalities are not subject to involuntary bankruptcy, and the federal Bankruptcy Code sets forth additional threshold requirements for municipal filings, above and beyond what would be required for most private entities.\textsuperscript{41} The accessibility of

\begin{itemize}
  \item \textsuperscript{35} Id. Notably, Alaska reported that twenty-nine percent of its cities could not pay debts on time. Id.
  \item \textsuperscript{36} Omer Kimhi, Reviving Cities: Legal Remedies to Municipal Financial Crises, 88 B.U. L. REV. 633, 647 (2008) [hereinafter Reviving Cities].
  \item \textsuperscript{37} Id.
  \item \textsuperscript{38} Id. at 648.
  \item \textsuperscript{39} Chapter 9 of the Bankruptcy Code, supra note 31, at 372. By contrast, once a municipality has entered bankruptcy, a court cannot compel it to increase tax rates. Id.
  \item \textsuperscript{40} See Reviving Cities, supra note 36, at 650.
  \item \textsuperscript{41} See McConnell & Picker, supra note 22, at 455. For example, to qualify, municipalities must meet a threshold test for insolvency, a requirement not imposed on private entities filing voluntary petitions. Id. at 455-56. Under the current insolvency test, a municipality must demonstrate that it has insufficient cash flow to be able to pay debts as they become due, and in contrast to private entity debtors, other assets and liabilities are not considered in this calculation. Id. at 456. The result of applying this stringent cash flow test is that a municipality will not qualify to file until it
Chapter 9 is also limited by constitutional concerns, most particularly the sovereignty reserved for the states under the Tenth Amendment. Thus, before a municipality may petition for Chapter 9 bankruptcy, the state must expressly and directly approve of the filing. Because the creditworthiness of other municipalities and the state itself may be negatively impacted by the bankruptcy filing of a single municipality, states have often been reluctant to give the required approval, and the second requirement can thus pose a significant impediment to municipal filings. Furthermore, a bankruptcy court's powers under Chapter 9 are limited to either confirming or rejecting a debt readjustment plan (without making modifications) because the court may not interfere with the local political or governmental affairs of the municipality. Thus, because the court's powers are limited in altering the plan, Chapter 9 bankruptcy offers municipalities a mode of debt readjustment through which they exhausts its borrowing power, and thus has assumed additional new debt.

42. See Christopher Smith, Comment, Provisions for Access to Chapter 9 Bankruptcy: Their Flaws and Inadequacy of Past Reforms, 14 BANKR. DEV. J. 497, 499-500 (1998). Federal bankruptcy courts have specifically cited state sovereignty concerns with regard to municipal bankruptcy filings. See, e.g., In re City of Colo. Springs, Spring Creek Gen. Improvement Dist., 177 B.R. 684, 693-94 (Bankr. D. Colo. 1995) ("Chapter 9 places federal law in juxtaposition to the rights of states to create and govern their own subdivisions."); In re Addison Cnty. Hosp. Auth., 175 B.R. 646, 649 (Bankr. E.D. Mich. 1994) ("A primary distinction between chapter 11 and chapter 9 proceedings is that in the latter, the law must be sensitive to the issue of the sovereignty of the states.").

43. See Reviving Cities, supra note 36, at 650. This requirement is premised on the Tenth Amendment's federalism principle that the federal government may not interfere with a state's political subdivisions without the state's consent. Nicholas McGrath & Ji Hun Kim, The Next Chapter for Municipal Bankruptcy, AM. BANKR. INST. J., June 2010, at 14-15.

44. See McConnell & Picker, supra note 22, at 460; see also, David R. Berman, Takeovers of Local Governments: An Overview and Evaluation of State Policies, PUBLIUS, Summer 1995, at 55, 59 (noting that states have generally been reluctant to allow municipalities to file for Chapter 9 bankruptcy, instead preferring that distressed municipalities utilize the remedies authorized by state legislation); Smith, supra note 42, at 521 (pointing out that because the credit ratings of other municipalities within a state are likely to be negatively affected by one municipality's filing, "one municipality's mess can become another's very real problem.").

45. Reviving Cities, supra note 36, at 653.
can "cram-down" unfavorable plans on reluctant creditors.\(^46\) Under this approach, creditors are the primary group to bear the cost of municipal insolvency, while the city is afforded an opportunity for a fresh, debt-free start.\(^47\) Finally, although the threat of bankruptcy may provide local actors with greater leverage in negotiations with creditors and unions, most municipalities eschew Chapter 9 filings because of the long-term damage that bankruptcy might cause to their credit ratings and ability to borrow at a low cost.\(^48\) For these reasons, municipal bankruptcy filings have been relatively uncommon.\(^49\) Overall, then, Chapter 9 bankruptcy provides an incomplete solution to the problem of municipal insolvency.\(^50\)

\(^{46}\) Id. at 651-52.

\(^{47}\) See id. at 654.

\(^{48}\) See Berman, supra note 44, at 58-59; see also, Chapter 9 of the Bankruptcy Code, supra note 31, at 383 (explaining that a municipality's financial crisis, "although seemingly an isolated event, may be a sign that more local crises will occur in the future," an issue encountered by Orange County after it filed for bankruptcy protection in the early 1990s).

\(^{49}\) See Robert J. Landry III & Keren H. Deal, More Municipalities Likely to Face Chapter 9: Is a Perfect Storm Brewing?, AM. BANKR. INST. J., Jul.-Aug. 2008, at 18, 18. Between 1938 and 2007, only 579 municipalities filed bankruptcy petitions, representing a "drop in the bucket" of total filings. Id. Moreover, the vast majority of municipal filings have been by "special-purpose municipalities," those designated to provide a specific service (e.g., utility districts). See Chapter 9 of the Bankruptcy Code, supra note 31, at 359 & nn.43-44. In fact, between 1976 and 2009, only forty general-purpose municipalities (i.e., towns, townships, cities, etc.) filed for Chapter 9 bankruptcy, and among those, only thirty were approved. Id. at 359. Two prominent municipal bankruptcy filings include that of Orange County, California in the early 1990s, and more recently the City of Vallejo's filing. See In re City of Vallejo, 403 B.R. 72, 74 (Bankr. E.D. Cal. 2009); In re County of Orange, 183 B.R. 594, 596 (Bankr. C.D. Cal. 1995).

\(^{50}\) Chapter 9 of the Bankruptcy Code, supra note 31, at 353-54. Kimhi argues that Chapter 9 "is not a sensible solution for urban economic crises, and that municipal financial distress should be dealt with in other manners." Id. In particular, Kimhi notes that while bankruptcy in a corporate context may be justified under the contract theory (i.e., that bankruptcy law eliminates the common pool problem, increasing the value obtained by creditors because creditors are considered collectively and the ones to benefit are not necessarily the first to the courthouse steps), or the fresh start theory (i.e., that giving an entity a fresh start, free from debt, will spark economic activity, thus leading to financial recovery), neither theory justifies municipal bankruptcy because there is no common pool problem in the municipal context and the underlying causes of a municipality's financial distress are unlikely to be eliminated along with its debts. Id. at 370-72.
State financial oversight boards offer a third avenue for resolution of municipal debt crises. Financial oversight boards originated before Congress passed municipal bankruptcy provisions, and are creatures of statute, vested with the power to restructure a municipality's debt and balance its budget. Research indicates that since the 1970s, state oversight boards have been utilized in at least fifty instances to resolve local fiscal distress. State financial oversight boards operate in one of two ways: in some instances state legislatures authorize oversight boards in response to a specific crisis (a reactive approach), while in other states, oversight boards assume a long-term monitoring role, continuously assessing the fiscal health of localities and intervening upon early indicators of distress (a proactive approach). Most often, however, the decision to create such a board is an ad hoc one, made after one or more municipalities have reached a crisis point. The use of financial oversight boards gives a city continued access to credit markets throughout the reformation process, and once the municipality's financial condition has sufficiently improved, the board typically dissolves and control returns to the regular governing entities. As discussed in detail below (see infra Part II), Rhode Island law has long provided for state intervention into municipal financial crises via financial oversight boards, although as the Central Falls experience demonstrates, the existence of such a remedy has not always prompted its proactive use.

51. Reviving Cities, supra note 36, at 654. Kimhi notes the dearth of academic or legal research and commentary on the role of financial oversight boards in resolving municipal insolvency, despite their apparent benefits. Id. at 636 & n.5.
53. See Berman, supra note 44, at 56. State intervention mechanisms have been utilized since the Great Depression, but New York City's 1975 financial crisis ushered in a modern era of state oversight. Id. at 60.
54. See Berman, supra note 44, at 57.
55. Reviving Cities, supra note 36, at 654. Often, states wait to intervene until a municipality's bond credit rating is downgraded significantly or it is unable to meet current operating expenses. Id.
56. See Reviving Cities, supra note 36, at 654.
C. Causes of Municipal Financial Distress and the Strengths of Various Remedies

Within the corporate context, insolvency is generally caused by either economic or financial distress. When a corporation's operating expenses are consistently higher than its revenues, economic distress occurs. By contrast, financial distress occurs as a result of a short-term inability to pay back debts, despite operating revenues. When a corporation is economically distressed, eliminating its debt through bankruptcy is unlikely to produce long-term recovery because its business model is not itself sustainable; however, when a corporation is financially distressed, eliminating burdensome debt obligations may allow the corporation a fresh start to begin to function profitably. Thus, in the corporate context, bankruptcy law protects financially distressed corporations by eliminating their onerous debt and allowing for the continued functioning of economically viable entities, while economically distressed corporations are allowed to fall by the wayside. In the corporate context, the distinction between economic and financial distress elucidates the situations in which bankruptcy will operate as an effective restructuring tool.

There are two primary theories as to what causes municipal financial distress. The first theory attributes municipal financial distress to extrinsic socioeconomic factors such as suburbanization, trends in the national economy, and larger taxing and spending policies. For example, some researchers

59. Id.
60. Id.
61. Id.
62. Id. at 375. Obviously, in the municipal context, allowing an economically distressed town or city to cease to exist would be an incomplete solution. Id.
63. Anthony G. Cahill & Joseph A. James, Responding to Municipal Fiscal Distress: An Emerging Issue for State Governments in the 1990s, 52 PUB. ADMIN. REV. 88, 92-93 (1992); see also Reviving Cities, supra note 36, at 638.
64. Reviving Cities, supra note 36, at 638-42. For example, unfunded mandates imposed by state governments can contribute significantly to a municipality's financial distress by creating additional costs and reducing the municipality's flexibility in making budgetary decisions. Chapter 9 of the Bankruptcy Code, supra note 31, at 377-78.
argue that a city's financial health depends on factors like "national business cycles, suburbanization and decline in local business activity, and state and federal policies towards local governments."65 In such contexts, restructuring, either via bankruptcy or state intervention is unlikely to resolve the long-term issues because ultimately, the cost of services that the municipality must provide to residents is simply too great to be satisfied through tax and other revenue.66 This theory on the factors underlying municipal insolvency is similar to the economic distress theory in the corporate context.

Conversely, the second approach attributes financial distress to political influences and mismanagement by local officials as the root causes of the problem. While theorists subscribing to this approach do not entirely discount the role of socioeconomic factors, they argue that "the city's political system is the ultimate determinant of whether the city will deteriorate into a crisis or will remain in relatively good fiscal health."67 For example, advocates of this theory sometimes point to poor or manipulative accounting practices by municipal managers as the ultimate cause of financial collapse.68 Others stress the role of political influences on elected officials, who are essentially held hostage by fragmented political interests groups.69 Under this view, theorists emphasize the disproportionate influence over municipal spending by small, specialized interest groups, who are able to utilize their political power to externalize the costs of their pet projects onto other taxpayers.70 Because these small but powerful political

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65. Reviving Cities, supra note 36, at 639.
66. Cahill & James, supra note 63, at 93. Some suggest that in such situations, the best solution is to annex the ailing municipality onto an economically stronger neighboring community. Id. However, this still does not alleviate existing contract and debt obligations or reduce the overall cost of services required for that community of residents. Id. Thus, annexation is likely to merely shift the problem, rather than resolving it. Id.
67. Reviving Cities, supra note 36, at 642.
68. See id. This theory seems to underlie the Orange County bankruptcy filing in 1994, where the municipality faced "acute and immediate" financial crisis after risky investments made by the municipality's finance director failed to pan out and the municipality lost an estimated $527 million. See In re County of Orange, 179 B.R. 177, 179 (Bankr. C.D. Cal. 1995); Landry & Deal, supra note 49, at 70.
69. Reviving Cities, supra note 36, at 643-44.
70. See id. at 644-45. Kimhi uses public swimming pools as an apt
interest groups are able to exert disproportionate influence over the budget process, local officials who are looking primarily to the next election cycle, rather than long-term sustainability, will be less likely to develop budget policies on the basis of informed economic judgment than they will be to respond to the immediate demands of those key constituents who exert substantial control over their political fates. For example, research indicates that municipalities that file for Chapter 9 bankruptcy often return to insolvency within a few years because the core problems created by fragmented special interests are not addressed by the bankruptcy remedy, and thus, long-term financial recovery is not achieved.

The ideal response to municipal financial crises may well depend on which of these theories operates in the case at hand. If the underlying cause of financial distress relates to socioeconomic patterns or external policies, then it may be unnecessary to remove the influence of politics in an effort to reform the budget. However, to the extent that political influences pervade the example of how such specialized interest groups achieve their intended policy outcomes while externalizing costs:

Usually, the costs of construction are taken from the public budget, but the pool will be used only by a specific segment of the community, i.e., those who like swimming and live relatively close to the pool. Nearby swimmers, therefore, have an incentive to pressure politicians to build a larger, more expensive pool. The swimmers will enjoy the pool's benefits, while the costs will be shared with the entire community.

*Id.* at 645.

71. *See generally* Ester R. Fuchs, Mayors and Money: Fiscal Policy in New York and Chicago 5-7, 242-61 (1992). Fuchs points to the power of fragmented political influences as the primary reason why New York experienced severe financial crises during the 1970s, while Chicago, another large city experiencing similar socioeconomic changes, did not. *Id.* at 5-7. Whereas the political scene in Chicago at that time was dominated by a strong political machine that could easily resist the political pressures of fragmented special interest groups, New York, on the other hand was not controlled by any single group, making it an ideal stage for political battles for control over the budget. *Id.*

72. *Chapter 9 of the Bankruptcy Code, supra* note 31, at 381. Although the restructuring benefit offered by Chapter 9 may help municipalities facing short-term and unexpected financial crises (e.g., rebuilding after a natural disaster or paying a large judgment in a lawsuit), when a city or town's financial distress is the result of long-term economic problems, bankruptcy reorganization offers little long-term assistance. *Id.* at 382.
budgetary process, removing some of the political pressure may be absolutely essential to developing and implementing the necessary changes to economic policy.\textsuperscript{73} In fact, unelected and politically unaccountable fiscal control boards may well be able to accomplish the budgetary overhaul necessary for long-term recovery precisely because they are not hindered by local political pressures.\textsuperscript{74} For example, when Chelsea, Massachusetts entered state authorized receivership in 1991, the receiver was able to negotiate a new contract with the firefighters' union that was favorable for the city, but unpopular with influential groups, "because the receiver did not have to run for re-election and face the wrath of organized, focused opposition."\textsuperscript{75}

Each of the three responses to municipal insolvency discussed above removes the influences of special political influences to some extent, and at the same time divests local residents of a democratic voice in the process. For example, in the context of traditional creditors remedies and bankruptcy, the authority of local officials over fiscal matters is substantially circumscribed, as the courts step in and play a significant role reshaping the municipality's obligations. Financial reform boards offer an opportunity to eliminate the destructive influences of political fragmentation, while still preserving some vestiges of democratic control over the reform process, and thus are the best option from the perspective of representational democracy.\textsuperscript{76} Although fiscal crisis typically requires a rapid damage control response,\textsuperscript{77} the

\textsuperscript{73} See Missed Opportunity, supra note 52, at 746-47. Some research indicates that centralizing budgetary authority in a single individual diminishes the role of special interest influences and the political fragmentation that can drive up deficits. See Reviving Cities, supra note 36, at 669.

\textsuperscript{74} Chapter 9 of the Bankruptcy Code, supra note 31, at 388-89.


\textsuperscript{76} See Missed Opportunity, supra note 52, at 734-35. This Note observes that as implemented in many U.S. jurisdictions, financial control boards deprive local residents of an appropriate role in the reform process despite the opportunity to integrate local input. See id.

\textsuperscript{77} For example, after New York City's financial crisis reached a fever pitch, "[l]ocal control was largely suspended during the 'crisis regime' as power over financial matters was vested in a small group of state appointees. Berman, supra note 44, at 60. Locally elected officials were largely frustrated in their efforts to influence the budgetary process for roughly a decade. Id.
immediate need for centralized control at the outset does not preclude the possibility of local input in later stages.\textsuperscript{78} For example, there is an immediate need in the face of such a crisis to stabilize a community's finances, giving reassurances to the municipality's creditors, as well as to credit rating agencies generally, so that the municipality can once again gain access to capital markets.\textsuperscript{79} However, once the initial stabilization has been accomplished, an opportunity opens to integrate resident stakeholders into the reform process, and, in fact, such a "full-blown fiscal crisis... can present voters with an incentive to participate meaningfully in decisionmaking that directly affects their quality of life."\textsuperscript{80}

Unfortunately, the typical implementation of financial control boards does not create opportunities for participation by the electorate, instead vesting control throughout the reform period in a politically unaccountable body, whose responsibility it is to resolve both the short and long-term crises.\textsuperscript{81} While this approach eliminates the pressures that fragmented and self-interested local factions exert under normal circumstances (those that may well have contributed to the fiscal crisis in the first place), excluding citizen participation beyond the initial damage control phase is neither necessary nor desirable.\textsuperscript{82} In fact, to the extent that continued monopolization of control over the budget reform process divests voter-residents of the chance to participate, this strategy robs them of a unique opportunity to gain "a sophisticated understanding of their role in the crisis and in potential future crises."\textsuperscript{83} Thus, by excluding voter-residents from the reform process, but later returning control to those who were in control pre-crisis, a state takeover fails as a teachable moment, entrenches the same local officials who were in power leading up to the financial collapse, and "undermines the significance of participatory decision-making as a democratic ideal."\textsuperscript{84} It appears, therefore, that utilizing a participatory process to resolve

\textsuperscript{78} See Missed Opportunity, supra note 52, at 746.
\textsuperscript{79} See id. at 739.
\textsuperscript{80} See id. at 745.
\textsuperscript{81} See id. at 746-47.
\textsuperscript{82} See id. at 746-47.
\textsuperscript{83} See id. at 747.
\textsuperscript{84} See id.
fiscal crisis not only creates an opportunity for the democratic input that we value as a society, but also serves to increase the likelihood of long term economic reform in economically stressed cities and towns.85

D. Preserving Local Control over Matters of Local Concern: The Home Rule Movement and Assurances of Democratic Control at the Local Level

Traditionally, American cities and towns have been thought to be creatures of the state.86 This idea is perhaps best captured by Dillon's Rule as articulated by Iowa Supreme Court Justice and legal scholar, John Dillon:

It is a general and undisputed proposition of law that a municipal corporation possesses, and can exercise, the following powers and no others: First, those granted in express words; second, those necessarily or fairly implied in, or incident to, the powers expressly granted; third, those essential to the declared objects and purposes of the corporation – not simply convenient, but indispensable. Any fair, reasonable doubt concerning the existence of a power is resolved by the courts against the corporation, and the power is denied.87

Inherent in this conception of municipal authority was the idea

85. See id. at 749. In an ideal fiscal reform process, “exposure to the fiscal issues facing the city through participation in the [financial reform board] process would enable citizens to begin developing the requisite knowledge to engage meaningfully in the political process in the future when fiscal matters are at issue.” Id.

86. For example, in Trenton v. New Jersey, the Supreme Court described the relative allocation of power between the state and municipalities, noting that:

The city is a political subdivision of the state, created as a convenient agency for the exercise of such of the governmental powers of the state as may be intrusted to it . . . . In the absence of state constitutional provisions safeguarding it to them, municipalities have no inherent right of self-government which is beyond the legislative control of the state . . . . the state may withhold, grant, or withdraw powers and privileges as it sees fit. 262 U.S. 182, 185-86, 187 (1923).

that cities and towns received limited grant of power from the state government, and that ultimately, the source of sovereignty over local matters rested with state, not the local government.\textsuperscript{88} As such, under Dillon’s Rule, a municipality’s reservoir of power was confined to express or implied grants of authority from the state to regulate in areas where local-decision making was “indispensable,” or the state had explicitly conferred a portion of its own plenary power on the lesser municipal government.\textsuperscript{89} In effect, Dillon’s Rule was a rule of statutory construction, which provided that “statutory grants of authority should be narrowly construed: if the grant contains an ambiguity, that ambiguity should be resolved against a finding of local government lawmaking authority.”\textsuperscript{90} Thus, Dillon’s Rule tended to reduce the amount of control that municipal officials could exercise over local affairs.\textsuperscript{91}

Although Dillon’s Rule had been accepted by most jurisdictions by the end of the nineteenth century, local politicians and municipal residents viewed the premise with suspicion as it allowed distant state legislatures to meddle in local affairs.\textsuperscript{92} After all, the Greek and Roman traditions, after which much of American government was modeled, preserved elements of local autonomy, and even the English Parliament had guaranteed certain liberties to localities.\textsuperscript{93} Thomas Jefferson himself had envisioned four hubs of republican government: the federal government to address foreign and federal issues, the state governments to legislate on matters of state concern, county governments to deal with county-wide issues, and finally, ward governments to address matters of neighborhood concern.\textsuperscript{94}

In the early twentieth century, the Home Rule Movement was

\begin{itemize}
  \item \textsuperscript{90} See Schwartz, supra note 88, at 1025.
  \item \textsuperscript{91} Id. at 1025.
  \item \textsuperscript{92} See Haas, supra note 89, at 680-81.
  \item \textsuperscript{94} Id. at 30.
\end{itemize}
born, finding its initial support among those local politicians and residents who sought to codify protection against the caprice of state legislators through Home Rule charters. Under Home Rule, municipalities received direct grants of authority in state constitutions, typically over local or municipal affairs, and these grants of authority effectively superseded Dillon’s Rule by vesting municipalities with their own identity and sphere of control, independent of the state. Home Rule is premised on the same basic principles that underlie federalism—the ideas that in some areas, a smaller, more localized government will be better situated to respond to local issues and that democratic input of the populace in resolving local problems contributes a unique value. As Barron points out:

The invocation of “local autonomy” conjures up the attractive values associated with protecting localized decisionmaking: promoting responsive and participatory government by bringing the government closer to the people; fostering diversity and experimentation by increasing the fora for expressing policy choices and creating a competition for a mobile citizenry; and providing a check against tyranny by diffusing power that would otherwise be concentrated.

Thus, a municipality’s right to Home Rule reflects not only a policy choice about the division of political power, but also the core values of our system of government that democracy can and should exist even at the most local level.

Home Rule provisions may serve dual functions: first, they may restrict the authority of state legislatures to pass laws regulating the form of municipal government (immunity provisions); second, they may confer upon municipalities the power to regulate a circumscribed set of matters without prior state authorization (initiative provisions). Most commonly,

96. Id. at 1026.
98. Id.
99. See Haas, supra note 89, at 682; Barron, supra note 97, at 392; U.S. ADVISORY COMM’N, supra note 93, at 7.
Home Rule provisions confer "grants of initiative," allowing localities to create and implement policies on local issues, but not necessarily limiting state intervention into local affairs.\textsuperscript{100} Many state constitutions, including Rhode Island's, contain a "ripper clause," which creates a negative local liberty by limiting the ability of the state to legislate on local structural issues (e.g., the form of local government) without approval by the local electorate.\textsuperscript{101} Home Rule provisions protect resident input at the local level by limiting the ability of the state government to dictate the form of local government and preventing state legislatures from dominating the minutia of day-to-day municipal activity.\textsuperscript{102} Therefore, Home Rule provisions enhance democratic functioning at the local level by ensuring that particular classes of locally enacted policies are afforded protection from state interference, while also conferring upon local governments a degree of legitimacy, vis-a-vis resident voters, and autonomy, vis-a-vis the state.

The tension between Home Rule on the one hand and Dillon's Rule on the other becomes apparent when considering solutions to inter-municipal problems. For example, trends like suburbanization and fluctuations in state and federal aid to municipalities tend not to exist in the vacuum of a single locality, so solutions to the problems caused by such inter-municipality trends often require an inter-municipal response.\textsuperscript{103} Furthermore, if towns and cities were completely free to craft and implement whatever policies best suited their residents, municipalities would likely externalize the costs of such policies, forcing their neighbors—equally autonomous localities—to bear the expenses.\textsuperscript{104} Thus, in some situations, centralized decision

\textsuperscript{100} U.S. ADVISORY COMM'N, supra note 93, at iii.
\textsuperscript{101} Id. at 12.
\textsuperscript{102} See Haas, supra note 89, at 682-83.
\textsuperscript{103} See Barron, supra note 97, at 378-79. Barron posits that "[t]he ability of each locality to make effective decisions on its own is inevitably shaped by its relation to other cities and states, by its relations to broader, private market forces, and, most importantly, by the way the central power structures these relations, even when central governmental power appears to be dormant." Id.
\textsuperscript{104} Id. at 385-86. Take, for example, air quality regulations: a locality that establishes lax air pollution standards for its residents may detrimentally affect air quality in neighboring municipalities, but those neighboring municipalities will be largely unable to mitigate the spread of
making may actually enhance local autonomy by limiting the ability of municipalities to implement policies that produce negative externalities for their neighbors.  

E. Rhode Island’s Home Rule Tradition

Rhode Island’s Home Rule history is particularly interesting because during much of the colonial era, Rhode Island was better categorized as a collection of cities and towns than as a unified colony. Even after Rhode Island received a charter from the throne in 1644, the centralized government was weak against the entrenched and independent settlements that predated the colony’s official existence. Eventually, a second charter was granted, authorizing a stronger centralized government, but it was several years before the General Assembly could wrest control from the politically powerful settlement communities because any shifts in control to the centralized colonial government were largely dependent on the consent of the decentralized communities. Even after the American Revolution, Rhode Island continued to operate under its colonial charter, and it was not until 1842 that the state adopted a constitution. Despite the early colonial tradition of strong, local self-government, by the early twentieth century it was clear that the primary reservoir of

the pollution.  *Id.* Without some centralized air pollution policy that constrains actors in all localities, the ability of the surrounding municipalities to control their own air quality is limited. *Id.* In such situations, therefore, a centralized policy that sets upper limits for local autonomy actually enhances the autonomy of localities on the whole. *Id.* at 386.

105. *Id.* at 386-87.

106. *See* SYDNEY V. JAMES, COLONIAL RHODE ISLAND: A HISTORY 1 (1975). In fact, Rhode Island began as four colonial settlements that eventually united under a colonial charter in 1647, but “[t]he form of government adopted under that charter was a federation of towns, rather than a colony. Legislation originated in the towns, and the general assembly had simply a power of approval or veto. Local self-government was preserved to its full extent.” City of Newport v. Horton, 47 A. 312, 313 (R.I. 1900).

107. Haas, *supra* note 89, at 687; see also City of Newport, 47 A. at 313.

108. Haas, *supra* note 89, at 688. Historical accounts describe this slow shift in control, noting that even as the General Assembly consolidated its own power, it engaged in the practice of granting town charters, which town leaders argued provided legal protection for particular aspects of local autonomy. *Id.* at 689.

109. *Id.* at 690.
power in Rhode Island rested with the General Assembly, and not the individual cities and towns. 110 Early Rhode Island Supreme Court decisions reflect the view that local communities lacked innate authority over local matters, and instead that the General Assembly was permitted to legislate on local matters. 111

By 1951, sufficient political support in favor of a Home Rule provision had accumulated, and the General Assembly adopted a Home Rule Amendment put forth at that year's limited constitutional convention. 112 The stated purpose of the amendment was to "grant and confirm to the people to the people of every city and town in this state the right of self government in all local matters." 113 The Amendment set specific limits on the power of the General Assembly to legislate on local matters:

§ 4. Powers of the general assembly over cities and towns:

The general assembly shall have the power to act in relation to the property, affairs and government of any city or town by general laws which shall apply alike to all cities and towns, but which shall not affect the form of government of any city or town. *The general assembly shall also have the power to act in relation to the property, affairs and government of a particular city or town provided that such legislative action shall become effective only upon approval by a majority of the qualified electors of the said city or town voting at a general or special*

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110. See id. at 691-92.

111. See, e.g., City of Providence v. Moulton, 160 A. 75, 75-76, 78 (R.I. 1932) (affirming state legislation that replaced locally appointed officials with a "Board of Public Safety," members of which were appointed by the governor, citing Dillon's Rule to support the conclusion that Rhode Island "cities and towns have no inherent right of local government"); City of Newport, 47 A. at 314, 316 (holding that while "[t]owns and cities are recognized in the constitution, and doubtless they have rights which cannot be infringed," Newport lacked the inherent right to completely control its police force, and the state legislature did not exceed its authority in establishing a board of police commissioners for the city).

112. R.I. CONST. art. XIII; Haas, supra note 89, at 692-93 (noting that the amendment passed the General Assembly unanimously with 170 votes in favor). Although the Home Rule Amendment was initially added to the state constitution as Article XXVIII, at the 1986 Rhode Island limited constitutional convention, the provision was moved to Article XIII. In re Advisory Op. to the House of Representatives, 628 A.2d 537, 538 (R.I. 1993).

113. R.I. CONST. art. XIII, § 1.
election, except that in the case of acts involving the imposition of a tax or the expenditure of money by a town the same shall provide for the submission thereof to those electors in said town qualified to vote upon a proposition to impose a tax or for the expenditure of money.\textsuperscript{114}

Thus, the Rhode Island Home Rule Amendment established an element of local democratic control, to be protected from certain state encroachments, by requiring changes that would affect the form of local government be approved by a majority of the municipality's voters before becoming effective.\textsuperscript{115} Furthermore, the Amendment provides that "every city and town shall have a legislative body composed of one or two branches elected by vote of its qualified electors," indicating that the Amendment was intended to protect not just local government, but a democratically elected local republican government.\textsuperscript{116}

Rhode Island's high court has addressed the Home Rule Amendment several times since its initial passage in 1951. These opinions fall into three general categories: advisory opinions issued per the request of the legislature, clarifying the applicability of the Amendment in particular factual contexts;\textsuperscript{117} challenges initiated by municipalities or their representatives,\textsuperscript{118} and judicial interpretations of the Amendment's provisions in specific cases.

\textsuperscript{114} Id. § 4 (emphasis added).
\textsuperscript{115} See id. However, to the extent that the General Assembly's legislation does not violate this or other constitutional provisions, it is supreme and thus preempts conflicting local ordinances. R.I. CONST. art. VI, § 1.
\textsuperscript{116} See R.I. CONST. art. XIII, § 3.
\textsuperscript{117} See, e.g., In re Advisory Op. to the House of Representatives, 628 A.2d at 539 (advising the state legislature that reapportionment of voting districts is among the powers reserved for a municipality under the Home Rule Amendment, and any state level approval of a reapportionment plan would trigger the voter ratification requirement described in section four of Article XIII because state approval would constitute state action affecting the form of local government); Op. to the House of Representatives, 96 A.2d 627, 630-31 (R.I. 1953) (concluding that the power to establish policies and procedures related to general municipal elections was retained by the General Assembly, and was not transferred to the municipalities via the Home Rule Amendment); Op. to the House of Representatives, 87 A.2d 693, 696 (R.I. 1952) (concluding that among several hypothetical scenarios posited by the General Assembly relating to state legislation that would affect local elections, only the imposition of term limits for municipal officials by the state legislature would constitute a regulation of the "form" of local government).
claiming that state legislation encroaches upon municipal legislative authority;\textsuperscript{118} and cases challenging municipal policies and regulations on the grounds that they are preempted by state law.\textsuperscript{119} Taken collectively, these decisions set forth several clear guidelines for determining the applicability of the Home Rule Amendment in any particular situation.

The first advisory opinion issued by the Rhode Island Supreme Court to the legislature following enactment of the Home Rule Amendment distinguished between the rights of those towns and cities that have passed a Home Rule charter, and those that have not, indicating that a validly enacted and approved charter is

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\item See, e.g., Marran v. Baird, 635 A.2d 1174, 1176, 1178-79 (R.I. 1994) (holding that the establishment of a budget commission with the power to impose taxes and make appropriations on behalf of a financially distressed municipality pursuant to state law did not violate Article XIII because the effect on local government was only "incidental and temporary," the legislation affected all cities and towns equally, and the provision addressed a matter of statewide concern); Town of East Greenwich v. O'Neil, 617 A.2d 104, 110-12 (R.I. 1992) (holding that the location of high-voltage power lines was a matter of statewide concern, and thus could be regulated by the state legislature notwithstanding local ordinances purporting to do the same); McCarthy v. Johnson, 574 A.2d 1229, 1230-32 (R.I. 1990) (holding that state legislation extending the period for giving notice of a tort claim against the City of Newport was invalid under Article XIII because it applied only to the City of Newport, not to all Rhode Island cities and towns generally, and it did not address a matter of statewide concern); Bruckshaw v. Paolino, 557 A.2d 1221, 1223-24 (R.I. 1989) (holding that Providence's pension plan for municipal employees was not a matter of statewide concern, such that the General Assembly's attempt to implement a competing plan for Providence employees encroached upon the city's home rule authority under Article XIII, and rendered the state legislation "invalid and unenforceable"); City of Cranston v. Hall, 354 A.2d 415, 417 (R.I. 1976) (holding that because the state-authorized Fire Fighters Act applied equally to all towns and cities, it did not violate Article XIII, and the state legislation therefore preempted local ordinances regulating the same activity).
\item See, e.g., O'Neill v. City of East Providence, 480 A.2d 1375, 1379-80 (R.I. 1984) (holding that where municipal and state procedures on condemnation were inconsistent, city officials were correct in following the state procedure because municipal laws that conflict with validly enacted state legislation are preempted); Marro v. Gen. Treasurer of the City of Cranston, 273 A.2d 660, 662-63 (R.I. 1971) (holding that actions taken by the mayor and city council to force a disabled police officer into retirement were invalid where a state statute purported to regulate the right of a disabled officer to receive a pension, reasoning that although cities and towns have the power to legislate on local matters under the Home Rule Amendment, local regulations that conflict with valid state legislation are preempted).
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a necessary precursor for Home Rule protections. Additionally, the Court made clear that when legislating on matters of local concern, the General Assembly may enact general measures that affect all cities and towns equally, but legislation directed at a particular city or town must be approved by a majority or resident-voters. The Court also indicated that the only absolute restraint created by the Home Rule Amendment on the General Assembly’s power is the prohibition against legislation that alters the form of government in a chartered town or city.

In an advisory opinion issued the following year, the Court read the powers conferred to municipalities narrowly, concluding that “all matters pertaining to the conduct of municipal general elections . . . are exclusively within the province of the general assembly and subject to existing general laws.” In reaching this conclusion, the Court emphasized the “long history of the general assembly’s exclusive authority over the conduct of elections,” and reasoned that had the framers of the Home Rule Amendment intended to vest authority to determine how municipal elections would be conducted with the municipalities themselves, they would have been more explicit in so doing. Thus, matters of local concern that the General Assembly have historically regulated are less likely to qualify for Home Rule protection.

Although early cases reflected a narrow reading of the Home Rule Amendment, the Court later broadened its reading of the

120. See Op. to the House of Representatives, 87 A.2d at 695-96. The Home Rule Amendment contains several provisions relating to the adoption and approval of town and city charters. See R.I. Const. art. XIII, §§ 6-10.
122. Id.
124. Id. at 630-31.
125. See, e.g., Newport Amusement Co. v. Maher, 166 A.2d 216, 218-19 (R.I 1960). In this early case, the Court invalidated a local ordinance requiring business with jukeboxes to obtain a city permit, reasoning that absent an express grant of power from the General Assembly, municipalities could not regulate in an area, refusing to recognize the Amendment as a “grant of plenary power to enact licensing laws without regard to the will of the legislature . . . .” Id. at 219. As Haas points out, “[t]he court here appeared not to consider the possibility that the Home Rule Amendment was in fact intended to confer upon municipalities a certain limited ability to enact regulations not inconsistent with those enacted by the General Assembly.” Haas, supra note 89, at 700.
provision, invalidating a handful of state laws that impermissibly impinged upon local autonomy. For example, in *Bruckshaw v. Paolino*, a 1989 case, the Court invalidated a state law purporting to establish a retirement system for Providence municipal employees. After Providence refused to implement one of the act’s provisions, an affected employee filed suit seeking declaratory relief. Holding that the state legislation encroached upon local decisional authority under the Home Rule Amendment, the Court set forth several guidelines for determining the situations in which the General Assembly has trespassed upon the decisional authority of local officials: a state provision will be “invalid and unenforceable” when (1) the town or city has adopted a charter that vests it with the authority to regulate the activity at issue, (2) the General Assembly has ratified the charter, (3) the state provision at issue purports to regulate a matter of local, as opposed to statewide concern, and (4) the state provision was not promulgated pursuant to Article XIII’s requirement that local matters be affirmed by a majority vote of the electorate.

Only a year later, in *McCarthy v. Johnson*, the Court again invalidated a state law on the grounds that it impermissibly interfered with local authority as reserved by the Home Rule Amendment. There, the plaintiff had failed to notify the City of Newport of a personal injury claim within the sixty-day notice period as provided by state law, and when the plaintiff eventually filed her lawsuit, Newport asserted, as its defense, the plaintiff’s failure to give timely notification of the claim. In response, the General Assembly passed a special act allowing the plaintiff at bar to give late notice in that case. In striking down this special exception, the Court noted that as in *Bruckshaw*, this statute “directly affect[ed] a single community,” and that as such, “it is a matter of local concern and must be submitted to the voters of that community at a general or special election” per the terms of the

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127. *Id.* at 1222.
128. *Id.* at 1222, 1224.
130. *Id.* at 1229-30.
131. *Id.* at 1230.
Home Rule Amendment.\textsuperscript{132}

The Court's decisions in \textit{Bruckshaw} and \textit{McCarthy} evince a reading of the Home Rule Amendment that gives a high level of deference to municipal autonomy against attempts by the state to intervene into the local affairs of a particular community. Similarly, in an advisory opinion to the House of Representatives only three years later, the Court affirmed the authority of a municipality to reapportion its voting districts under the Home Rule Amendment without the approval of the General Assembly.\textsuperscript{133} In fact, noting that the "Legislature can act only in relation to the property, affairs, and government of any home-rule city or town by the General Laws when such legislation pertains to all cities and towns alike and does not affect the form of government of any home-rule city or town," the Court concluded that any such approval or input by the General Assembly would constitute state action affecting the form of local government, and would require approval by a majority of the municipality's voters.\textsuperscript{134} Taken together, this line of cases demonstrates a departure from the Court's narrow construction of the Home Rule Amendment that was typical in its earlier jurisprudence.\textsuperscript{135} In fact, through these cases, the Court seems to have embraced the underlying goals of the Home Rule Amendment: promoting local control over local matters, but with a balance against the plenary authority of the General Assembly to legislate on matters of statewide concern.\textsuperscript{136}

\textsuperscript{132} \textit{Id.} at 1231. The Court later set forth three criteria in ascertaining whether a matter is of local as opposed to statewide concern: whether uniform statewide regulations are necessary or desirable, whether the matter has traditionally been left to the state or to localities to address, and whether the matter will affect other communities. \textit{Town of East Greenwich v. O'Neil}, 617 A.2d 104, 111 (R.I. 1992).

\textsuperscript{133} \textit{In re Advisory Op. to the House of Representatives}, 628 A.2d 537, 539 (R.I. 1993).

\textsuperscript{134} \textit{Id.} at 538.

\textsuperscript{135} \textit{Haas, supra note} 89, at 707.

\textsuperscript{136} \textit{Id.} (positing that "[t]he result [from this line of cases] has not been a complete destruction of the legislature's authority . . . between the state and home rule municipalities in a strictly limited number of areas."). In fact, when local residents challenged a municipality's authority to expand its own sewer system under under its Home Rule charter, the Court held that while "[m]unicipalities may not [ ] legislate on matters of statewide concern," "the power over sewers and drains is not a matter of statewide concern since [the town's] charter specifically provides for the department of public works to be
Of particular importance in assessing the state's response to Central Falls' financial crises was the Court's decision in *Marran v. Baird.*\(^{137}\) There, the City of West Warwick was at risk of defaulting on its bond obligations and its bond credit rating had been downgraded to junk bond status, triggering the formation of a budget commission under the precursor statute to the current municipal insolvency legislation.\(^{138}\) The plaintiffs in that case challenged the validity of the budget commission that was constituted to balance the city's budget, arguing that because the legislation that authorized the budget commission would affect every municipality differently, it did not apply "alike" to all cities and towns as required by the Home Rule Amendment.\(^{139}\) Furthermore, the plaintiffs argued that because the imposition of a budget commission would alter the form of municipal government, voter approval was required before the change could take legal effect.\(^{140}\)

The Court rejected both arguments, finding that because the statute allowed for the appointment of a budget commission ""in any town or city"" upon specified triggering events, while the statute affected each town and city differently, it applied equally to all.\(^{141}\) Moreover, the Court noted that because ""[t]he fiscal collapse of a municipality can affect the entire state's financial interests,"" the General Assembly has traditionally played an active role in ""ensuring financial stability [of cities and towns] notwithstanding the provisions of the home-rule charters.""\(^{142}\) As to the plaintiffs' argument that the statute impermissibly altered the form of local government, the Court held that because the commission's role would last only through the remainder of the

\(^{137}\) Marran, 635 A.2d 1174 (R.I. 1994).

\(^{138}\) Marran v. Baird, 635 A.2d 1174, 1176 (R.I. 1994). As described further below, at that time, the formation of a budget commission was the only mechanism through which a state could intervene in a municipal financial crisis. See R.I. GEN. LAWS § 45-9-3(a)(1) (1956), amended by R.I. GEN. LAWS §§ 45-9-1 to -17 (2010).

\(^{139}\) Marran, 625 A.2d at 1177.

\(^{140}\) Id.

\(^{141}\) Id. (quoting R.I. GEN. LAWS § 45-9-3, amended by R.I. GEN. LAWS § 45-9-1 to -17 (2010)).

\(^{142}\) Id. at 1178-79.
fiscal year, the statute's "effect on the structure of West Warwick's government [wa]s at most incidental and temporary," and "[t]he provision d[id] not, therefore, affect the form of government of any city or town and consequently d[id] not violate article 13." 143 Thus, while the Court had previously recognized and protected the ability of municipalities to legislate on matters of local concern, it drew a line here, allowing for state intervention when a municipality's financial condition posed a risk to other communities. The Court's "temporary and incidental" qualifier thus allows for direct state intervention into the form of a municipality's government so long as the alteration is not permanent or sweeping, evincing a less deferential interpretation of the Home Rule Amendment under which even the form of local government is not sacred when the matter at hand threatens other Rhode Island communities.

II. ANALYSIS

A. Rhode Island's Financial Oversight Statute

In 1993, Rhode Island implemented a state-level financial oversight provision whereby upon certain triggering events, the state's director of revenue would become empowered to intervene and establish a budget commission. 144 Under this statute, the director of revenue had the authority to unilaterally establish a budget review commission upon a finding that the municipality's bond credit rating had been downgraded to below investment grade and "there [wa]s an imminent threat of default on an one or all of its debt obligations." 145 Budget commissions were to be composed of a mix of state representatives and local stakeholders including the municipality's chief executive officer, the president of its town or city council, three residents of the municipality, and two ex-officio state officials. 146 Review boards were empowered to impose taxes, make appropriations, adopt a budget, and reduce or

143. Id. at 1178.
145. Id.
146. Id. § 45-9-3(a)(2). One of the ex-official state officials would be a designee and representative of the director of revenue, and the other a gubernatorial appointee, with the advice and consent of the state Senate. Id.
suspend appropriations to specific departments.147 Boards could act upon a simple majority, so long as a quorum of four was achieved.148 The structure of the budget review commission under the 1993 legislation preserved an important element of local control by setting a high threshold for state intervention, integrating both local officials and municipal residents, and allowing for majority control by a body that was primarily comprised of local, as opposed to state, stakeholders. Although the Court did not specifically mention the high level of local participation on the budget review commission in its decision in Marran, the fact that the commission was controlled by local stakeholders may have contributed to the Court's determination that the statute's impact on the form of local government was only "incidental."149

Despite signs of financial distress in Central Falls leading up to its judicial receivership petition, the budget commission statute was not triggered because Central Falls' bond credit rating was not downgraded to below investment grade until after the municipality filed for receivership.150 At that point, the perception among state officials was that stronger medicine was needed.151 The General Assembly rushed into action, hastily passing a bill that would alter the existing budget commission provision and incorporate additional mechanisms for state oversight of municipal finances.152

This sweeping new legislation is intended to “provide a mechanism for the state to work with cities and towns undergoing financial distress that threatens the fiscal well-being, public safety and welfare of such cities and towns, or other cities and towns or the state.”153 Furthermore, the authority conferred by the legislation is to be utilized “in such a manner as will best preserve the safety and welfare of citizens of the state and their property, and the access of the state and its municipalities to capital

147. Id. § 45-9-3(a)(9).
148. Id. § 45-9-3(a)(6).
150. City in Receivership, supra note 1; Ratings agency, supra note 7.
152. State reviewing, supra note 11.
markets, all to the public benefit and good."\(^{154}\) In order to accomplish these policy goals, the legislation establishes a three-tier mechanism for state intervention, allowing the state to provide "varying levels of support and control depending on the circumstances."\(^{155}\)

The lowest level of state intervention is the appointment of a fiscal overseer, who is designated by the state director of revenue either upon the request of the municipality's chief executive officer and council, after consulting with the auditor general, or unilaterally should the director of revenue find that any two of several triggering events have occurred and "threaten the fiscal well-being of the city or town, diminishing the city or town's ability to provide for the public safety or welfare of the citizens."\(^{156}\) The primary role of the fiscal overseer is to examine the municipality's budget and make recommendations to local officials as to what steps are appropriate or necessary to restore budget stability.\(^{157}\) Overall, the fiscal overseer provision in the new legislation is consistent with the ideals of local self-government embodied in the Home Rule Amendment because it

\(^{154}\) Id.

\(^{155}\) Id. §§ 45-9-1, -3, -5, -7. In evaluating the constitutionality of the statute, a Rhode Island Superior Court characterized this as a "five-tier mechanism," including within its framework two possible outcomes following state intervention: the creation of a municipal department of administration and finance following resolution of the immediate fiscal crisis, or alternatively, authorization for the town or city to file for Chapter 9 bankruptcy should the state intervention prove ineffective. See id. §§ 45-9-7, -10; Pfeiffer, C.A. No. PB 10-5615, at 10-11, 14-15. Because this Comment focuses on the state's initial intervention in response to municipal financial crisis, it will treat the provisions of the Act as establishing three levels of intervention, with two exit mechanisms rather than characterizing the scheme as the Superior Court did in Pfeiffer. See id.

\(^{156}\) R.I. GEN. LAWS § 45-9-3(a)-(b) (2010). Triggering events include, a municipality projecting a deficit for the current and coming fiscal years or failing to file timely audits with the state for two successive years, downgraded bond status or inability to access credit markets, or a failure to properly respond to requests made by state officials regarding fiscal conditions. Id. § 45-9-3(b).

\(^{157}\) Id. § 45-9-3(d). Among the powers given to the overseer are recommending fiscal policies, supervising financial services and activities, advising the municipality's fiscal officers, providing assistance with financial matters, assisting with the development of a municipal budget, reviewing contracts, monitoring expenditures, approving annual and supplemental budgets, and reporting progress to the director of revenue. Id.
does not displace local decision-makers, leaves intact mechanisms for holding those local officials accountable, and achieves a level of state-municipal collaboration that does not undermine the role of local input in resolving local financial problems.

The second level of state intervention involves appointment of a budget commission by the director of revenue.\textsuperscript{158} Although this mechanism existed in the previous legislation, it is substantially revised under the new statute.\textsuperscript{159} For example, the new legislation expands the range of triggering events for the creation of a budget review commission, allowing the director of revenue to establish such a commission upon the recommendation of the fiscal overseer or upon a finding by the overseer that the municipality will be unable to present a balanced budget, faces a fiscal crisis that poses an imminent threat to residents, will be unable to achieve financial stability without the assistance of a budget commission, or that the tax levy should not be approved.\textsuperscript{160} Additionally, the director of revenue must establish a budget commission if the state's division of municipal finance notifies her that a municipality is unable to achieve a balanced budget, and she may establish a budget commission if a municipality's chief executive officer and council jointly request one.\textsuperscript{161} Thus, under the new legislation, a wider variety of events may trigger the establishment of a budget review commission, and rather than relying exclusively on clear and objective indicators of municipal financial distress (i.e. downgraded credit status and immediate inability to meet pending obligations) as the prior legislation had, the new statute relies on less objective indicators of financial distress, while also providing a greater opportunity for early intervention.\textsuperscript{162} While this early intervention approach is favored by bond-rating agencies because it calms fears that Rhode Island law makes it too easy for municipalities to file for bankruptcy,\textsuperscript{163}

\begin{footnotes}
\item[158] \textit{Id.} § 45-9-5.
\item[161] Id. § 45-9-5(f).
\item[162] Then-Governor Carcieri praised the new legislation for exactly this reason – it allows for state intervention "at the first sign of trouble." Randal Edgar, Carcieri OKs receivership guidelines law, PROVIDENCE J., June 15, 2010, at A5.
\item[163] See id.
\end{footnotes}
it also provides an opportunity for the state to interfere in local affairs at a much earlier stage, and with fewer objective indicators of financial distress than under the previous legislation.

Additionally, under the revised legislation, budget review commissions are dominated by state-appointed members, in contrast with the prior statute, which provided for commissions that were primarily comprised of local officials and residents.\footnote{R.I. GEN. LAWS § 45-9-3(a)(2) (1956), amended by R.I. GEN. LAWS §§ 45-9-1 to -17 (2010); R.I. GEN. LAWS § 45-9-6 (2010).} Now, the five member commission (down from seven) is made up of a municipality's chief executive officer, the president of the town or city council, and three designees of the director of revenue, all appointed without the input of the state legislature.\footnote{R.I. GEN. LAWS § 45-9-3(a)(2) (1956), amended by R.I. GEN. LAWS §§ 45-9-1 to -17 (2010); R.I. GEN. LAWS § 45-9-6 (2010).} However, because the commission still acts by majority vote, effective control under the new statute has been shifted from local stakeholders to state appointees. Furthermore, by eliminating the three positions on commissions reserved for municipal residents, the new statute eliminates a unique opportunity for local input and participation in the budget reformation process. Finally, whereas under the old statute the state Senate approved the appointment of a commission member, the new statute no longer requires that check.

The powers of a budget commission are largely the same under the new statute as they were previously, with one important caveat: if the budget commission concludes that its intervention will be insufficient it can recommend to the director of revenue that a receiver be appointed, at which point the director of revenue is required to act upon the commission's suggestion.\footnote{R.I. GEN. LAWS § 45-9-7 (2010).} Thus, a commission that is controlled by individuals appointed by a single member of the executive branch without input from the legislature is empowered under the statute to make a unilateral determination that receivership is necessary to resolve a municipality's budget crisis. Obviously, such a concentration of decision-making authority in the hands of an unelected outsider poses a threat to local control over important issues such as municipal taxing, spending, and service provision.

At the highest level of state intervention, the director of
revenue may appoint a receiver, who steps into the shoes of the municipality’s top officials, displacing locally-elected leaders, and assumes responsibility for the day-to-day operation of the municipality, as well as budget reformation efforts. Receivership may be triggered in one of two ways: first, as described above, upon the recommendation of the budget review commission to the director of revenue that a receiver is necessary to resolve the municipal financial crises, or alternatively, if the director of revenue determines that the municipality is facing a “fiscal emergency” and “circumstances do not allow for appointment of a fiscal overseer or a budget commission,” she may utilize the statute’s emergency provision and install a receiver immediately. This was the provision utilized in Central Falls’ case, whereby the director of revenue appointed a receiver to replace the temporary receiver who had been appointed by the Superior Court. Under the statute, the receiver has:

The power to exercise any function or power of any municipal officer or employee, board, authority, or commission, whether elected or otherwise relating to or impacting the fiscal stability of the city or town including, without limitation, school and zoning matters.

Thus, receivership under the statute virtually eliminates local input into the day-to-day operation of a municipality, instead vesting complete control in an unelected official who is appointed by a member of the state’s executive branch upon either a finding of “fiscal emergency” or the recommendation of a state-dominated budget review commission. Clearly, this mechanism divests voters of their right to local self-government, potentially achieving a greater level of financial stability, but at the cost of democratic decision-making.

167. See id.
168. Id. § 45-9-7 to -8.
169. Pfeiffer, C.A. No. PB 10-5615, at 28 n.27.
171. For example, upon assuming control in Central Falls, the state-appointed Receiver demoted the mayor to an “advisory” role, explaining that “[y]ou can’t have two leaders.” John Hill, New administrator swiftly takes control, PROVIDENCE J., July 20, 2010, at A1. Within months, the receiver completely disbanded the city council, instead instituting an “Advisory Panel” made up of what critics call “yes-men,” whose attitudes are politically and ideologically aligned with the Receiver’s own views. John Hill, Receiver
B. Reconciling Home Rule Ideals with the Need for Fiscal Stability

Rhode Island's new fiscal oversight statute, particularly as implemented in Central Falls' case, impinges on the authority of locally-elected municipal officials to design and implement local policy on behalf of their constituents. Furthermore, at the higher levels of intervention, especially receivership, the statute deprives local residents of a voice in the governance of their cities and towns, displacing locally-elected officials, as well as the municipality's governmental and political structures, and instead vesting centralized control in a state-appointed and politically unaccountable individual. Thus, it appears that the statute, at least as it was applied in Central Falls' case, defies the Home Rule Amendment's prohibition against altering the form of local government without the approval of resident-voters. However, when the Mayor and members of the Central Falls City Council challenged that law on these grounds, a Rhode Island Superior Court justice concluded that the law, even as applied in Central Falls, did not violate the Home Rule Amendment.172

The court first addressed the claim that because the statute was enacted retroactively to a date only four days before Central Falls initially filed for judicial receivership, "it applie[ts] exclusively to Central Falls, and should have been subject to a vote of the electorate in accordance with the Home Rule Amendment."173 However, applying the Marran framework, the court concluded that regardless of whether the Act, by virtue of its retroactive application, affected Central Falls differently than it affects other Rhode Island municipalities, "on its face and by its terms the Act applies equally to all cities and towns, including Central Falls, and is therefore a statute of general application."174

172. Pfeiffer, C.A. No. PB 10-5615, at 47-48. The Mayor and City Council members challenged the law on several other grounds as well, arguing that it violates the separation of powers and non-delegation doctrines, and that as applied here, it violated the substantive and procedural due process rights of Central Falls' elected officials. Id. at 29, 31, 35, 38. The court rejected each of these claims. Id. at 48.
173. Id. at 20.
174. Id. at 20-21.
Next, the court addressed arguments by the mayor and city council that because the statute was aimed at Central Falls' fiscal crises, it "fails to address an issue of statewide concern."175 However, applying the standards set out in Marran, Brancato, and Town of East Greenwich, the court concluded that:

Where, as here, Rhode Island has consistently exercised oversight over municipal budgets and debt obligations, the insolvency of a city or town threatens the credit of the state and other cities and towns, and uniform regulations are desirable and necessary to protect the fiscal stability of the state and its municipalities, . . . the Act affects matters of statewide concern.176

In other words, given the threat posed by Central Falls' precarious financial situation to surrounding communities, and the General Assembly's traditional role overseeing municipal financial issues, the state had a clear and legitimate interest in intervening.177

Finally, the court addressed the argument that the Act impermissibly altered the form of municipal government in Central Falls by displacing a variety of appointed and elected officials without first obtaining the necessary approval from the voters.178 The court noted that under the Home Rule Amendment, "the General Assembly has no right to alter or amend a municipality's form of government," but applying the Marran analysis, it concluded that "although the Receiver's powers are broad and the receivership is not limited to a particular durational term, the Act does not permanently affect a municipality's form of government," and therefore does not violate the Home Rule Amendment.179

It would seem, then, that this case is controlled by Marran insofar as Home Rule is concerned, and thus that the statute does not infringe upon the constitutionally guaranteed rights of municipal officials and their residents to be free from undue interference by the state in matters of local concern.180

175. Id. at 21-23.
176. Pfeiffer, C.A. No. PB 10-5615, at 22-23.
177. Id. at 22.
178. Id. at 23.
179. Id. at 25-26.
180. The Superior Court's decision has been appealed, and the Rhode Island Supreme Court heard oral arguments on February 1, 2011. Court
C. Democratic Input and the Long-Term Sustainability of Local Fiscal Reform

Even assuming that Rhode Island's new fiscal oversight provision does not violate any component of the Home Rule Amendment, its application in this case reflects hastily-made public policy choices that fail for three primary reasons to adequately serve the underlying goal of promoting long term financial stability in Central Falls. First, as applied in this case, implementation of the statute via the emergency receivership provision deprived Central Falls residents of a voice in the process, offending the underlying ideals of the Home Rule Amendment. To the extent that the intervention utilized here "den[ies] residents any opportunity to participate meaningfully in the decisionmaking process," it "send[s] the unmistakable message that democratic control is ineffective and that the city residents are incapable of making difficult decisions." This message is in diametric opposition to the democratic values underlying the Home Rule Amendment.

Second, by eliminating the involvement of local stakeholders in the process, the likelihood only increases that such a fiscal disaster will occur again in Central Falls. For instance, if this financial emergency was the result of political influences – interest group pressures, externalized costs, or other factors that are uniquely tied to the democratic process – by eliminating local officials from the reform process, the state has eliminated the need for those local officials to minimize or ameliorate negative political pressures as they manifest themselves in the budgetary process. On the other hand, if Central Falls' fiscal crisis was caused not by poor fiscal management, but by independent socioeconomic factors like a decreasing tax base or suburbanization, utilizing a transparent reform processes in which the electorate can participate will also have longer lasting effects, as residents will have a greater opportunity to own and understand the financial problems facing their city, and participate in the difficult decision-making process that is

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hears appeal, supra note 21. As of the date of this writing, the Rhode Island Supreme Court had not yet issued a decision in this case.

181. See Missed Opportunity, supra note 52, at 750.
essential to a long-term resolution.

Third, if poor financial management is to blame for the current state of Central Falls' budget, the state has eliminated important political accountability mechanisms by excluding local officials from the reform process. For example, the current Mayor and City Council can criticize the actions of the Receiver, deflecting whatever blame the voters would have otherwise attributed to them. Thus, by replacing local government actors with a non-politically accountable manager, the state has significantly hindered the political process as a mechanism for dealing with fiscal mismanagement.

III. RECOMMENDATIONS

Here, the state waited until the fiscal crisis in Central Falls had escalated, and then, in a flurry of legislative activity, hastily passed a statute giving the director of revenue almost complete authority to displace an entire local government in one fell swoop. However, the writing was on the wall in Central Falls, and with consistent, regimented oversight, the state likely could have averted the crisis at a much earlier stage. Certainly, Central Falls' ongoing fiscal problems were no mystery; had the proper monitoring mechanisms been in place, the state could have stepped in at an earlier point, precluding the need for such a drastic intervention. Indeed, the complete elimination of democratic control might not even have been necessary.

As noted above, state responses to municipal fiscal struggles

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182. For example, when the General Assembly convened the Central Falls Review Commission in 1991 to evaluate Central Falls' then-existing financial crises, the Commission cited a litany of chronic factors contributing to the City's economic struggles:

The City's current problems stem directly from its history, geography, and demography, and its excessive reliance on property taxes as the source of locally-derived revenues. Although many specific decisions of the past can be questioned, the city inevitably reached the point at which its property tax base had no more room to grow, while its expenses continued to increase. Several cost-saving measures and tax increases postponed, but could not ultimately avoid, today's problems. These are of course exacerbated by the fact that the City's people have the lowest average income in the state.

tend to be either reactive or proactive.183 One of the most significant flaws in reactive policies is that they often lack early warning systems to detect distress before an actual crises occurs.184 Research reveals that at least nine states have implemented proactive monitoring and early response systems for municipal financial distress.185 In a study of these nine states, Coe identified three best practices adopted by state governments: monitoring systems that facilitate the prediction of fiscal distress, early assistance to struggling municipalities to prevent the situation from worsening, and strong authority to require (rather than merely request) remedial action be taken by the municipality.186 Coe found that the states that implemented all three of these strategies were in the best position to detect and prevent financial distress, warding off major crises.187 States with early warning systems monitor a wide variety of indicators of financial health, but researchers have identified nine key variables that may be predictive of pending financial distress: population growth, real taxable value growth, large real taxable value decrease, general fund expenditures as a percentage of taxable value, general fund operating deficit, prior general fund operating deficits, size of general fund balance, fund deficits in the

183. Berman suggests that reactive, rather than proactive interventions by state oversight boards are in fact “more consistent with the assumption that local governments should conduct their own affairs and devise solutions to their own problems,” because under the reactive approach, the state becomes involved only after local officials have failed to effectively ward off crisis, and the state’s role is therefore more limited. See Berman, supra note 44, at 68. Conversely, Berman asserts that a proactive approach implies ongoing supervision by state actors, which “may lead to greater local controversy because it is uninvited and more directly conflicts with the norm of local autonomy.” Id. However, while the supervisory role of state officials necessary under a proactive approach may prove an annoyance to local officials who seek to make local fiscal decisions unencumbered by state oversight, proactive monitoring and early intervention is unlikely to lead to the wholesale loss of local control by preventing the acute financial crisis that may trigger a reactive and extreme intervention.


185. Coe, supra note 34, at 760. These include Florida, Kentucky, Maryland, New Hampshire, New Jersey, New Mexico, North Carolina, Ohio, and Pennsylvania. Id. at tbl. 1.

186. Id.

187. See id.
current or previous year, and general long-term debt as a percentage of taxable value. 188

As an alternative to the hasty and late intervention utilized by the Rhode Island state government in response to Central Falls' insolvency, Rhode Island should embrace an early intervention model, like the one used in North Carolina. 189 North Carolina's system was initially devised during the Great Depression, and emphasizes ongoing state oversight of municipal finances and early, but limited, intervention. 190 North Carolina's approach adopts all three of the best practices described by Coe and is considered to be a model in the United States: that state has the most municipal units receiving top credit scores anywhere in the country. 191 Moreover, since 1932, North Carolina's state-level oversight agency has been required to takeover municipalities in only four instances. 192 North Carolina's success is largely attributable to its comprehensive and sophisticated monitoring system, whereby a state agency consistently evaluates the financial health and debt management of local governments, watching for early warning signs. 193 Municipalities are also required to submit semi-annual financial statements to the state monitoring agency, and must obtain state approval before issuing local debt. 194 Given this consistent and comprehensive

188. Kloha et al., supra note 184, at 317-19. Weighing each variable and applying the scale to Michigan's municipalities, the authors found that this metric correctly identified three financially distressed municipalities that were eventually taken over by the state. Id. at 319.

189. See Reviving Cities, supra note 36, at 679.

190. See Coe, supra note 34, at 761.

191. See Reviving Cities, supra note 36, at 679; Coe, supra note 34, at 761. Not only does North Carolina's state-level monitoring agency carefully review financial reports submitted by municipalities on a regular basis, but it also requires state approval for the issuance of new bonds and provides immediate assistance to municipalities whose financial reports show warning signs of distress. Id. at 761-62.

192. Coe, supra note 34, at 763. To put this figure in perspective, North Carolina's oversight agency continuously monitors approximately 1,100 municipalities for signs of financial distress. See id. at 760 tbl. 1.

193. Reviving Cities, supra note 36, at 679-80. Kimhi acknowledges that when municipal financial crises reach a level that requires state takeover, local autonomy is necessarily sacrificed, albeit temporarily. Chapter 9 of the Bankruptcy Code, supra note 31, at 390. However, to the extent that ongoing oversight prevents the escalation of crises the net impact of continuous oversight is likely less detrimental to local autonomy and decision making.

monitoring, the state is able to identify warning signs at an early stage, and work closely with local officials to resolve budgetary issues before they snowball out of control.\textsuperscript{195} In fact, when the Fitch IBCA Rating Agency reviewed North Carolina's procedure in 1999, it concluded that "[t]he frequency and thoroughness of review by the [state's monitoring agency], coupled with its record of assuming fiscal control before stress leads to crisis, provides additional credit strength to most local issuers."\textsuperscript{196} North Carolina's proactive approach and constant "surveillance" of municipal finances appears to have achieved unparalleled success in preventing the type of municipal fiscal crises that requires immediate and sweeping state intervention.\textsuperscript{197} A corollary benefit to North Carolina's oversight approach is that by reducing the risk of catastrophic financial crisis among municipalities and increasing creditor confidence, interest rates available for municipal borrowing are lower, creating an overall costs savings.\textsuperscript{198}

As compared to the recent ex-ante intervention of the Rhode Island state government into Central Falls' budget crises, a proactive approach preserves local control over local issues by minimizing the need for large-scale state intervention.\textsuperscript{199} Certainly a statute mandating regular fiscal reports from all Rhode Island towns and cities would not violate the Home Rule Amendment, and its interference with local government would be

\textsuperscript{195} Id.
\textsuperscript{197} Id. at 683 (quoting Richard P. Larkin & Jeff Schaub, \textit{State of North Carolina Local Government Commission: Credit Enhancement Program Review}, FITCH IBCA TAX-SUPPORTED SPECIAL REPORT, Mar. 29, 1999, at 5).
\textsuperscript{198} Chapter 9 of the Bankruptcy Code, supra note 31 at 394. Because creditors trust that North Carolina's oversight agency will step in to prevent a default, they are also more willing to lend money to the state's municipalities, and at a lower interest rate, saving the state's municipalities millions of dollars every year. \textit{Id}.
\textsuperscript{199} In fact, when the General Assembly authorized the Central Falls Review Commission in the early 1990s, the body's role was "to work \textit{with} City officials and assist in solving problems; not to perform any of the functions of the Mayor, City Council, or School Committee." \textit{CENTRAL FALLS REVIEW COMM'N, supra} note 182, at 4 (emphasis added). Thus, it is obvious that a state takeover is not the only viable solution to municipal financial crises in Rhode Island.
minimal from a democratic integrity standpoint. In fact, mandating such reporting and oversight might actually enhance transparency at the local level, providing resident-voters with an additional method for evaluating the performance of their local officials. Such an approach would also allow for more limited intervention at the early stages of financial distress, through which local policy makers could retain at least some authority to act on behalf of their constituents. In the long run, ongoing supervision will not only contribute to enhanced local autonomy by limiting the need for sweeping, emergency intervention, but it will also contribute to greater municipal financial health overall, and consequently lower interest rates for all of Rhode Island’s municipalities.200

IV. CONCLUSION

Whether or not Rhode Island’s new financial oversight statute violates the Home Rule Amendment as applied in this case, it certainly does not comport with the underlying ideals of local democratic government embodied in the Amendment. To the extent that the receivership provision precludes local input and participation in the budget reform process, it undermines the democratic process and is thus unlikely to produce lasting change. Although no other Rhode Island municipalities have reached the same crisis point as Central Falls,201 fiscal mismanagement at the local level poses a threat to all of Rhode Island’s towns and cities, and must be managed or controlled in some way by the state. However, rather than implementing rushed, ex-ante responses, the state, its municipalities, and their citizens would be better served by a proactive approach.

201. At the time Central Falls first filed for receivership, at least two other Rhode Island municipalities – Woonsocket and North Providence – faced similarly severe financial distress, although neither had reached the same crisis point as Central Falls. See City in Receivership, supra note 1. As of the writing of this Comment, state officials were working with three distressed municipalities in addition to Central Falls, prompting the House Speaker to suggest that “Central Falls may not be just the odd black swan, it may actually be the canary in the mine shaft.” Randal Edgar, Central Falls is the tip of the iceberg, PROVIDENCE J., Jan. 9, 2011, at A1.