
In the Matter of the Rehabilitation of:

Segregated Account of Ambac Assurance Corporation

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Case No. 10 CV 1576

**BRIEF IN OPPOSITION TO WELLS FARGO'S MOTION TO MODIFY TEMPORARY
INJUNCTION ORDER AND TO INTERVENE**

**Wisconsin Office of the Commissioner of Insurance and
Sean Dilweg, Commissioner of Insurance of the State of Wisconsin,
as Rehabilitator of the Segregated Account of Ambac Assurance Corporation**

INTRODUCTION

The motion of Wells Fargo Bank, N.A. ("Wells Fargo"), in its capacity as trustee for certain bondholders of the Las Vegas Monorail Company ("LVM"), to "Modify Temporary Injunction Order and to Intervene" seeks neither to modify the temporary injunction order nor to intervene. Indeed, nowhere in Wells Fargo's brief in support of its motion does it identify *any* provision of this Court's Temporary Injunction Order that it seeks to modify, and nowhere does Wells Fargo even contend that it has a right to intervene in this proceeding.¹

¹ Wells Fargo's only asserted ground for intervention is paragraph 12 of this Court's Order for Temporary Injunctive Relief, which states in relevant part: "If any interested parties believe any portion of this Order is unwarranted by the facts or the law, such parties may seek modification or dissolution of part or all of this Order by filing a written motion . . ." (Dkt. 9, ¶ 12.) That paragraph grants no right to formally intervene in these proceedings, as this Court previously recognized in denying other policyholders' motions to intervene for failure to satisfy the requirements for intervention under Wisconsin law. (Dkt. 136, Conclusions ¶ 9.) Further, as noted above, that paragraph does not even apply to Wells Fargo's motion because the motion does not identify any portion of the injunction order that it seeks to modify or dissolve.

Wells Fargo instead raises five separate legal challenges relating to the formation of the Segregated Account of Ambac Assurance Corporation (the “Segregated Account”). This Court has already addressed four of those challenges—whether the formation of the Segregated Account was invalid under (1) Wisconsin statutory law, (2) the Wisconsin common law of contracts, (3) the Takings Clause of the United States Constitution, or (4) the Due Process Clause of the United States Constitution—and ruled in favor of the Wisconsin Office of the Commissioner of Insurance (“OCI”), as regulator of Ambac and Rehabilitator of the Segregated Account, as to each. (*See generally* Court’s Findings of Fact and Conclusions of Law, dated May 27, 2010 (hereinafter “Findings” and “Conclusions”) (dkt. 136).) As Wells Fargo has acknowledged, the motion before the Court at that hearing “addresse[d] the Segregated Account Disputes and track[ed Wells Fargo’s] Motion almost verbatim with respect to those disputes.” (Dkt. 121, ¶ 3.) There is no question that the Court reached those questions, and that it considered Wells Fargo’s position in deciding them. (Transcript of May 25, 2010 Hearing, dkt. 127, at 121:18-122:22, 129:2-8.) Wells Fargo has not moved this Court for reconsideration of its decision regarding those four issues. Therefore, OCI adopts and incorporates its prior response on these matters (dkt. 83-88) and submits that Wells Fargo has presented no grounds for questioning this Court’s prior decision.

Wells Fargo’s sole remaining challenge is that OCI violated the Equal Protection Clause when it approved the establishment of a segregated account that included policies insuring LVM bonds. This argument is meritless. As described below, to prevail on an Equal Protection challenge, Wells Fargo must show that there was no conceivable, rational basis for OCI to distinguish between policies insuring the LVM bonds and policies insuring other risks when it approved the Segregated Account allocations. Wells Fargo’s single page of briefing on

this argument does not recognize—let alone attempt to meet—this heavy burden. (Wells Fargo Br. at 16.) Nor could it. As described in the May 20, 2010 Affidavit of Roger A. Peterson (dkt. 85), which was submitted to this Court in connection with OCI’s opposition to numerous motions challenging the establishment of the Segregated Account and a now-finalized settlement with several banks, the allocation of LVM policies to the Segregated Account was the product of a well-informed, rational decision-making process designed to preserve claims-paying resources, fairly protect all policyholders in the long run, and effect the rehabilitation of a major insurer without needless collateral damage. OCI’s distinction between policies with “imminent and substantial” anticipated claims, as Wells Fargo characterizes the LVM policies (Wells Fargo Br. at 16), and policies without such expected liabilities, is permitted by law and hardly irrational in light of Ambac’s financial outlook and OCI’s statutory duties.

BACKGROUND

Beginning in late 2007, the financial stability of Ambac Assurance Corporation (“Ambac” or the “General Account”) began to deteriorate as numerous financial instruments it insured suffered significant actual and expected future losses. (Findings ¶ 3; Peterson Aff. ¶ 3.) As Ambac’s claims payments and projected loss impairments mounted and its liquid claims-paying resources were eroded over the next two years, it became increasingly clear to OCI that some type of regulatory action under Chapter 645 of the Wisconsin Statutes would be necessary to slow the current and projected short-term outflow of Ambac’s claims-paying resources. (Findings ¶ 19; Peterson Aff. ¶ 8.) Without taking action to stop this substantial short-term drain on assets, there was a growing risk that Ambac would become insolvent before its in-force policy obligations were satisfied. (*Id.*)

Ambac's deteriorating financial condition left OCI with two realistic regulatory choices: (1) place all of Ambac into a Chapter 645 rehabilitation proceeding, or (2) allow Ambac to establish the Segregated Account, allocate certain troubled policies to the Segregated Account while leaving most policies in Ambac's General Account, and commence rehabilitation of the Segregated Account. (Findings ¶ 20; Peterson Aff. ¶ 9.) Based on extensive regulatory analysis, OCI determined that placing Ambac as a whole into a rehabilitation proceeding would trigger material damages to the detriment of all policyholders, cause substantial and uncontrollable collateral damage to third parties (including companies with performing commercial asset-backed security transactions such as Dunkin' Donuts, Sonic, and Hertz), and create unpredictable and unnecessary risks to the broader economy, among other adverse consequences. (Findings ¶¶ 21-24; Peterson Aff. ¶ 9(a).) A full-blown rehabilitation of Ambac, with its accompanying harms, was wholly unnecessary to serve the purposes of rehabilitation; the vast majority of Ambac's policyholders had (and continue to have) problem-free policies with little or no projected claims payments, and therefore did not imminently threaten to drain Ambac's claims-paying resources. (Findings ¶ 21; Peterson Aff. ¶ 9(a)(v).)

Therefore, OCI opted for a more surgical, individualized approach to rehabilitation by identifying those policies for which formal rehabilitation would prevent likely harm to Ambac and its policyholders as a whole, allocating those policies to a segregated account established under Wisconsin law, and commencing rehabilitation of the Segregated Account. (Findings ¶¶ 25-27; Peterson Aff. ¶ 9(b).) The 14,000-plus policies that were without material projected losses, that carried risks of collateral damage that outweighed the benefits of rehabilitation, and/or that were subject to binding agreements to forbear from exercising certain contractual triggers were left in the General Account. (Findings ¶ 31; Peterson Aff. ¶ 12.)

The allocation decisions were premised on the above-noted considerations, rather than the pursuit of a clean split placing public-finance policies in the General Account and structured-finance policies in the Segregated Account. (Findings ¶ 30; Peterson Aff. ¶ 14.) Indeed, of the roughly 1,000 policies ultimately allocated to the Segregated Account prior to the commencement of rehabilitation, around 200 were either direct public-finance policies or swap surety policies with public-finance components. (*Id.*) Conversely, the large number of structured finance transactions that were performing were left in the General Account, together with performing public-finance policies. (Peterson Aff. ¶ 15.) To date, the Ambac has paid less than \$10 million in claims with respect to the approximately 14,000 policies in the General Account. (Findings ¶ 31; Peterson Aff. ¶ 12.)

The LVM policies were allocated to the Segregated Account because, as Wells Fargo acknowledges, their anticipated claims are “imminent and substantial” (Wells Fargo Br. at 16) and thus threatened to drain Ambac’s liquid claims-paying resources before its in-force policy obligations were satisfied (Findings ¶ 19; Peterson Aff. ¶ 8). Indeed, the present value losses associated with LVM exposure could exceed \$350 million—one of the highest projected individual deal losses in the Segregated Account, and more than 35 times the combined losses of the roughly 14,000 policies in the General Account to date. (Findings ¶¶ 29, 31; Peterson Aff. ¶¶ 12-13.)

LVM filed for Chapter 11 bankruptcy in Nevada in January 2010. (Findings ¶ 29.) The United States Bankruptcy Court for the District of Nevada recently held that LVM was entitled to file for bankruptcy under Chapter 11, as opposed to the Chapter 9 bankruptcy provisions applicable to public debtors, because LVM is not a municipality within the meaning of the Bankruptcy Code. *In re Las Vegas Monorail Company*, No. BK-S-10-10464-BAM, 2010

WL 1857241 (Bankr. D. Nev. Apr. 26, 2010) (attached). The bankruptcy court differentiated LVM from more traditional municipalities or public financing boards or districts by noting that LVM is “a private corporation under applicable Nevada law,” it “exercises no traditional public powers,” it “bears the consequences of its operations in a manner similar to a private entity,” and that a “key component of the transaction, known to all, was that the State of Nevada would not be liable on the Bonds.” *Id.* at *1, *2 n.4, *23-24; *see also* Peterson Aff. ¶ 14 n.2.

ARGUMENT

The facts summarized herein and described in more detail in the Peterson Affidavit make it abundantly clear that the decision to allocate the LVM policies to the Segregated Account was the result of deliberate, well-reasoned consideration by OCI, taking into account Ambac’s financial state, OCI’s statutory duties, and the financial and policy analysis of OCI and its advisors. Far from the application of authority “with an evil eye and unequal hand,” as Wells Fargo contends (Wells Fargo Br. at 16), OCI’s allocation of the LVM policies to the Segregated Account was entirely rational and warranted by the law.

A. The Allocation of the LVM Policies to the Segregated Account Did Not Violate the Equal Protection Clause.

The Equal Protection Clause of the United States Constitution² does not render unconstitutional any government action that makes distinctions among individuals, groups, beneficiaries of insurance policies, or, as in this case, the insurance policies themselves. So long as the distinction does not impair a fundamental right—which any government actions “[i]n the area of economics and social welfare” do not—or a “suspect class,” courts will uphold the

² The state Equal Protection Clause and the federal Equal Protection Clause are interpreted identically. *State v. Post*, 197 Wis. 2d 279, 317 n.21, 541 N.W.2d 115, 128 n.21 (1995). Therefore, this brief addresses only the federal Equal Protection Clause.

classification drawn if “any state of facts reasonably may be conceived to justify it.” *Dandridge v. Williams*, 397 U.S. 471, 485 (1970) (emphasis added, internal quotation omitted). Even if it results a disparity in treatment, “[s]uch a classification cannot run afoul of the Equal Protection Clause if there is a rational relationship between the disparity of treatment and some legitimate government purpose.” *Heller v. Doe*, 509 U.S. 312, 320 (1993).

Wells Fargo’s Equal Protection challenge to the allocation of LVM policies to the Segregated Accounts fails for at least three reasons. *First*, it targets the wrong classification. Allocation decisions were not made on the basis of whether the policy at issue insured municipal bonds, privately issued securities, interest rate swaps, collateralized debt obligations of asset-backed securities, or any of the other unique, complicated investments for which Ambac issued financial guaranty policies. Indeed, given the wide variety and complex nature of many of the obligations Ambac insured, such a classification system would have been nearly impossible to implement. The LVM policies offer a prime example. The LVM bonds are similarly situated to public finance bonds in that they raised revenue for a public transit project, but they are also similarly situated to private structured financing obligations in that the entity obligated to pay them has “no traditional public powers” such as the power to tax and “bears the consequences of its operations similar to a private entity.” *In re Las Vegas Monorail*, 2010 WL 1857241, at *23-24. They are, like most of the transactions Ambac insures, unique and not readily capable of clean categorization based on the characteristics of the underlying obligation.

Further, any attempt to allocate policies according to such a classification inevitably would be over- or under-inclusive in serving the purposes of protecting policyholders, because the characteristics of the underlying obligation are not necessarily relevant to whether the policy at issue threatened Ambac’s ability to pay claims or presented collateral damage

concerns. It would make no practical sense to allocate an entire group of similarly structured collateralized debt obligation deals to the Segregated Account just because some of those deals included *ipso facto* triggers, nor would it make practical sense to keep that same group of deals in the General Account simply because other of those deals would cause needless collateral damage if allocated to the Segregated Account. The classification system Wells Fargo suggests is hopelessly imprecise and inefficient.

Therefore, the classification OCI drew was whether the policies had material projected losses and/or triggers that jeopardized Ambac's liquid claims-paying resources and thus put all Ambac policyholders at risk, regardless of whether the financial guaranty policies in question insured an obligation from a municipality, a corporation, or anything else. In light of OCI's statutory mission to protect policyholders and the public while rehabilitating financially distressed insurers, Wis. Stat. § 645.01(4), that classification is hardly irrational.

Second, the LVM policies squarely fit that classification. Despite Wells Fargo's repeated implication that other policyholders in the Segregated Account are somehow different because they have policies insuring "toxic risks" (Wells Fargo Br. at 1, 5, 16), its own concession that LVM claims are "imminent and substantial" places LVM policies firmly within that category. Indeed, the potential losses associated with LVM exposures represent one of the highest projected deal losses in the Segregated Account. (Findings ¶ 29; Peterson Aff. ¶ 12.) Thus, the LVM policies are similarly situated to other policies allocated to the Segregated Account.

Third, Wells Fargo has not and could not argue that OCI has unlawfully treated policies within that category (*i.e.*, policies allocated to the Segregated Account) differently from each other. All Segregated Account policyholders are subject to the claims moratorium currently

in place, and they will all be bound by the terms of the rehabilitation plan upon its approval. Further, it is wholly unclear how the formation of the Segregated Account has resulted in disparate treatment for LVM policy beneficiaries even as compared to General Account policyholders. As noted above, all policyholders benefit from the rehabilitation proceeding in that it protects Ambac's liquid resources from an inefficient and inequitable "run on the bank," to the detriment of those policyholders who suffer losses beyond the near-term. To move the LVM policies to the General Account and allow LVM policy beneficiaries to recover "substantial and imminent" losses in full and in cash as they accrue, while other policyholders have either performing obligations that do not incur losses or policies that are subject to the rehabilitation proceeding, would unfairly favor the LVM beneficiaries at the expense of all other policyholders of Ambac.

Finally, it should be noted that even if Wells Fargo had a right to discovery—which it does not—discovery could not cure the infirmities of Wells Fargo's Equal Protection challenge. OCI is under "no obligation to produce evidence to sustain the rationality" of its Segregated Account classifications or to even "articulate at any time the purpose or rationale supporting its classification." *Heller v. Doe*, 509 U.S. 312, 320 (1993) (quotation omitted). "Instead, a classification must be upheld against equal protection challenge if there is any reasonably conceivable state of facts that could provide a rational basis for the classification." *Id.* (quotation omitted). Ambac's financial state and the need to prevent an uncontrolled and inequitable outflow of claims paying resources provides an entirely rational basis for segregating policies with "imminent and substantial" anticipated claims in order to proceed with a targeted rehabilitation proceeding.

B. Wisconsin Law Does Not Prohibit OCI from Approving the Segregated Account.

In addition to being wholly rational, the classification OCI made when determining Segregated Account allocations was also authorized by Wisconsin law. Section 611.24 of the Wisconsin Statutes permits insurers to establish an optional segregated account “for any part of its business” subject to OCI approval, which must be granted unless OCI finds that the segregated account would be “contrary to the law or to the interests of any class of insureds.” Wis. Stat. § 611.24(2). As noted in its letter approving the establishment of the Segregated Account, OCI found that the Segregated Account was lawful and served the best interests of Ambac’s only “class of insureds”—policyholders of financial guaranty insurance.³ (Findings ¶ 26; Peterson Aff. ¶ 9(b)(i) Ex. 1.)

Wisconsin law requires the establishment of segregated accounts for certain classes of insurance business if an insurer also engages in other classes of insurance business, Wis. Stat. § 611.24(1), but nothing in the *optional* segregated account provision requires segregation of accounts by class of insurance, Wis. Stat. § 611.24(2). If otherwise, OCI would be unable to approve the establishment of any segregated account for Ambac, because it offers only one class of insurance. Section 611.24(2) does not make that distinction, nor does it require a monoline insurer to create sub-classes of insurance based on undefined, arbitrary characteristics of the insured risk such as whether it insures the obligations of a municipality, a corporation, or some other entity or person, as suggested by Wells Fargo. Instead, Section 611.24(2) allows the establishment of a segregated account for “any part” of an insurer’s

³ As noted in Wis. Stat. § 611.24(1)(am), the Wisconsin legislature characterizes financial guaranty insurance as a specific “class of insurance business.” Ambac, as a “monoline” insurer, engages in only this class of insurance business, as opposed to casualty, life, or other lines of insurance business.

business and “provides for optional segregated accounts *under any circumstances the corporation wishes*, if the separation meets the commissioner’s approval.” Wis. Stat. Ann. § 611.24 & cmt. (1971) (emphasis added). OCI approved the creation of the Segregated Account here for the part of Ambac’s business that met the criteria described in the Peterson Affidavit, and OCI’s findings in its approval letter had “strong factual support and [we]re not clearly erroneous or contrary to the weight of the evidence.” (Findings ¶ 26.) Therefore, nothing in Wells Fargo’s claim of unlawful discrimination calls into question the Court’s prior conclusion that the “Segregated Account was formed in compliance with Wisconsin law.” (Conclusions ¶ 2.)

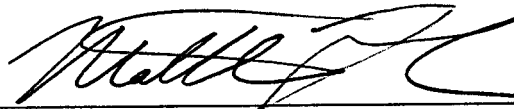
CONCLUSION

For the reasons stated above, Wells Fargo’s Motion to Modify Temporary Injunction Order and to Intervene should be denied.

Dated this 10th day of June, 2010.

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--- B.R. ---, 2010 WL 1857241 (Bkrcty.D.Nev.)
(Cite as: 2010 WL 1857241 (Bkrcty.D.Nev.))

HOnly the Westlaw citation is currently available.

United States Bankruptcy Court,
D. Nevada.
In re **LAS VEGAS MONORAIL COMPANY**, Debtor.
No. **BK-S-10-10464-BAM**.

April 26, 2010.

Background: Creditor moved to dismiss Chapter 11 case on ground that debtor, a nonprofit corporation that owned and operated a 3.9 mile long monorail which connected certain Las Vegas hotels, qualified as “instrumentality of the state” and was required to proceed under Chapter 9 rather than Chapter 11.

Holding: The Bankruptcy Court, Bruce A. Markell, J., held that nonprofit corporation that was not created pursuant to statute, did not have any traditional government powers such as those of taxation, eminent domain or sovereign immunity, and did not rely on public fisc to support its operations but on fares collected from its customers, did not qualify as “instrumentality of the state,” and thus was not rendered ineligible for Chapter 11 relief.

Motion denied.

West Headnotes

[1] Statutes 361 212.6

361 Statutes
361VI Construction and Operation
361VI(A) General Rules of Construction
361k212 Presumptions to Aid Construction
361k212.6 k. Words Used. Most Cited


Cases

Starting point for all statutory interpretation is presumption that Congress intended the accepted and plain meaning of words that it used.

[2] Statutes 361 188

361 Statutes
361VI Construction and Operation
361VI(A) General Rules of Construction

361k187 Meaning of Language
361k188 k. In General. Most Cited Cases


Statutes 361 223.1

361 Statutes
361VI Construction and Operation
361VI(A) General Rules of Construction
361k223 Construction with Reference to Other

Statutes


361k223.1 k. In General. Most Cited Cases

To discern Congressional intent, courts look to existing statutory text and not to predecessor statutes.

[3] Statutes 361 181(2)

361 Statutes
361VI Construction and Operation
361VI(A) General Rules of Construction
361k180 Intention of Legislature
361k181 In General
361k181(2) k. Effect and Consequences.

Most Cited Cases

Statutes 361 188

361 Statutes
361VI Construction and Operation
361VI(A) General Rules of Construction
361k187 Meaning of Language
361k188 k. In General. Most Cited Cases

When statute's language is plain, sole function of courts, at least where the disposition required by statutory text is not absurd, is to enforce it according to its terms.

[4] Statutes 361 188

361 Statutes
361VI Construction and Operation
361VI(A) General Rules of Construction
361k187 Meaning of Language
361k188 k. In General. Most Cited Cases

In construing statute, courts generally look to the ordinary meaning of statutory terms.

[5] Bankruptcy 51 2021.1

--- B.R. ---, 2010 WL 1857241 (Bkrcty.D.Nev.)
(Cite as: 2010 WL 1857241 (Bkrcty.D.Nev.))

51 Bankruptcy

51I In General

51I(B) Constitutional and Statutory Provisions

51k2021 Construction and Operation

51k2021.1 k. In General. Most Cited Cases

Courts should not read the Bankruptcy Code to erode past bankruptcy practice, absent clear indication that Congress intended such a departure. 11 U.S.C.A. § 101 et seq.

[6] Bankruptcy 51 ⚡2232

51 Bankruptcy

51III The Case

51III(B) Debtors

51k2222 Who May Be a Debtor

51k2232 k. Municipalities. Most Cited

Cases

First factor that bankruptcy courts consider in deciding whether entity is “municipality,” of kind ineligible to file Chapter 11 petition and required to seek bankruptcy relief under Chapter 9, is whether it has any of powers typically associated with sovereignty, such as eminent domain, taxing power or sovereign immunity; if entity has traditional government powers or engages in traditional government functions, then it is likely a municipality. 11 U.S.C.A. §§ 101(27,40,41), 109(d).

[7] Bankruptcy 51 ⚡2232

51 Bankruptcy

51III The Case

51III(B) Debtors

51k2222 Who May Be a Debtor

51k2232 k. Municipalities. Most Cited

Cases

If traditional governmental powers are lacking or only weakly present in entity, then court, to determine whether it nonetheless qualifies as “municipality” of kind ineligible to file Chapter 11 petition, considers whether entity has public purpose/function or attributes that reflect a public purpose and extent to which state controls the implementation of those functions and attributes. 11 U.S.C.A. §§ 101(27,40,41), 109(d).

[8] Bankruptcy 51 ⚡2232

51 Bankruptcy

51III The Case

51III(B) Debtors

51k2222 Who May Be a Debtor

51k2232 k. Municipalities. Most Cited

Cases

If there is state control coupled with public function, nature and extent of that control determine whether entity is “instrumentality of the state” and thus a “municipality,” so as to be ineligible for Chapter 11 relief and required to seek bankruptcy relief under Chapter 9; if control retained or exercised is necessary or designed to allow state to manage its finances or its fisc, then entity is “instrumentality of the state,” but if control retained or exercised is more akin to oversight or regulation, then entity is not such an instrumentality. 11 U.S.C.A. §§ 101(27,40,41), 109(d).

[9] Bankruptcy 51 ⚡2232

51 Bankruptcy

51III The Case

51III(B) Debtors

51k2222 Who May Be a Debtor

51k2232 k. Municipalities. Most Cited

Cases

While not determinative, some deference is given to state's categorization of entity in deciding whether it is “instrumentality of the state,” of kind ineligible for Chapter 11 relief. 11 U.S.C.A. §§ 101(27,40,41), 109(d).

[10] Bankruptcy 51 ⚡2232

51 Bankruptcy

51III The Case

51III(B) Debtors

51k2222 Who May Be a Debtor

51k2232 k. Municipalities. Most Cited

Cases

Representation by putative debtor, for purpose of establishing tax exempt status of interest earned on bonds issued to provide funding for expansion of its monorail system to serve certain Las Vegas hotels, that it qualified as “instrumentality of the state” for federal tax purposes was not determinative of whether it also qualified as “instrumentality of the state,” as that term was used in definitional provisions of the Bankruptcy Code dealing with what it meant to be “governmental unit” ineligible for Chapter 11 relief and required to seek relief under Chapter 9. 11 U.S.C.A. §§ 101(27,40,41), 109(d).

[11] Statutes 361 ⚡209

--- B.R. ---, 2010 WL 1857241 (Bkrcty.D.Nev.)
 (Cite as: 2010 WL 1857241 (Bkrcty.D.Nev.))

361 Statutes

361VI Construction and Operation

361VI(A) General Rules of Construction

361k204 Statute as a Whole, and Intrinsic Aids to Construction

361k209 k. Same or Different Language.

Most Cited Cases

Word used in one federal statute does not necessarily have the same meaning when used in another federal statute that does not cross reference the first.

[12] Bankruptcy 51 ↪ 2232

51 Bankruptcy

51III The Case

51III(B) Debtors

51k2222 Who May Be a Debtor

51k2232 k. Municipalities. Most Cited

Cases

While, if entity is not “instrumentality of the state” for federal tax purposes, it is quite likely not an “instrumentality of the state” for bankruptcy purposes, the obverse is not necessarily true. 11 U.S.C.A. §§ 101(27,40,41), 109(d).

[13] Bankruptcy 51 ↪ 2232

51 Bankruptcy

51III The Case

51III(B) Debtors

51k2222 Who May Be a Debtor

51k2232 k. Municipalities. Most Cited

Cases

Nonprofit corporation that owned and operated a 3.9 mile long monorail which connected certain Las Vegas hotels, that was not created pursuant to statute, did not have any traditional government powers such as those of taxation, eminent domain or sovereign immunity, and did not rely on public fisc to support its operations but on fares collected from its customers, did not qualify as “instrumentality of the state” or “municipality,” and thus was not rendered ineligible for Chapter 11 relief, where corporation, while subject to certain amount of state control in that state had authority to approve its fares and budget, and to appoint its directors, was in charge of its day-to-day operations in significant isolation from the state; such control as state had went to the service corporation provided to general public and not to protection of public fisc, and Nevada law did not treat corporation as one of its instrumentalities. 11 U.S.C.A. §§ 101(27,40,41), 109(d). Erika Pike Turner, Gabrielle A. Hamm, Matthew C. Zirzow, Gordon & Silver, Ltd., Gerald M. Gordon, William M. Noall, Las Vegas, NV, for Debtor.

ORDER REGARDING AMBAC'S MOTION TO DISMISS

BRUCE A. MARKELL, Bankruptcy Judge.

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I. INTRODUCTION

*1 Las Vegas Monorail Company ("LVMC"), the debtor and debtor in possession in this case, owns and operates a 3.9 mile long monorail which connects nine hotels in Las Vegas. LVMC seeks to serve the transportation needs of the Las Vegas resort corridor, and caters mostly to tourists and other visitors to Las Vegas. The monorail, however, does not connect to the local airport, and it does not connect to Las Vegas' downtown area. While it does connect to the local convention center, the closest it gets to the

principal thoroughfare in Las Vegas, the Las Vegas Strip, is approximately 1,000 to 1,500 feet.

LVMC's somewhat complicated capital structure, and its disappointing ridership, has hampered its ability to expand to better serve its goals. LVMC's immediate predecessor was a joint venture between two local hotels. Starting in 1998, this predecessor took advantage of a change in Nevada law that allowed private companies to operate a public monorail, and obtained a franchise from the local county government to operate the then-one-mile-long monorail. In 2000, the private joint venture sought to expand to its present length. As part of that expansion, the

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joint venture merged with a nonprofit corporation to form the present LVMC.^{FN1} LVMC then arranged for structured financing to acquire the existing track and to expand it.

The financing required the participation of the Director ("Director") of the Nevada Department of Business and Industry ("Department"). This participation consisted of the Director's sponsoring the issuance of around \$650 million of municipal bonds ("Bonds"). These Bonds were offered for sale pursuant to an Offering Statement dated September 12, 2000 (the "Offering Statement").^{FN2} Specifically, the Bonds were issued under an indenture ("Indenture") between Wells Fargo Bank ("Trustee") and the Director. The financing then called for the Director to simultaneously lend the bond proceeds to LVMC pursuant to a separate financing agreement between LVMC and the Director (the "Financing Agreement"). Under the Financing Agreement, the Director lent the bond proceeds to LVMC, and LVMC agreed to repay the loan. It supported its promise with a grant of a security interest in, among other things, its net revenues (but not in any of its track or trains).

A key component of the transaction, known to all, was that the State of Nevada would not be liable on the Bonds. Indeed, the Director and other public officials assured the public that no tax revenues would be used to acquire or operate the monorail. Structurally, this promise was honored by making the Bonds nonrecourse as to the State of Nevada. This was explicit in the offering; the only recourse for bondholders was the collateral the Director assigned to the Trustee, and the insurance mentioned below.

As a result, those buying the Bonds did so knowing that the primary source of repayment on the Bonds was the Financing Agreement-and the security interests it contained-which the Director had assigned to the Trustee. The only other potential source of repayment was insurance purchased from Ambac Assurance Corp. ("Ambac") which insured payment of principal and interest on the first series of the Bonds.

*2 This type of financing-called variously conduit financing or industrial revenue bond financing or special revenue financing-is a common way to finance municipal infrastructures. It is expressly recognized by the Internal Revenue Code. See 26 U.S.C. § 103. It allows a State or municipality to secure financing for the construction and operation of enterprises with a public purpose while offer-

ing tax-free interest to buyers of the bonds issued as part of the transaction. As part of this effort to obtain tax exempt status, LVMC signed a "Tax Certificate and Agreement" (the "Tax Certification") which expressly states that LVMC "is an instrumentality of the State of Nevada, ... controlled by the Governor of the State of Nevada."^{FN3}

As time passed, the payments on the Bonds proved to be too much for LVMC to service from its revenues. LVMC's ridership has never met projections; many of its potential patrons use services provided by the Regional Transportation Commission ("RTC"), a public agency charged with meeting the transportation needs of most of Las Vegas's residents. This is not to say that LVMC bleeds money; to the contrary, its revenues exceed its expenses,^{FN4} with more than \$5 million annual profit before debt service. This \$5 million, however, is barely enough to cover 10% of the scheduled debt service on the Bonds.

To address its financial distress, LVMC filed for Chapter 11 bankruptcy protection on January 13, 2010. Within hours of its filing, Ambac moved to dismiss LVMC's case. Ambac contends that LVMC is a "municipality" as defined by the Bankruptcy Code, and therefore ineligible to file anything other than a Chapter 9 bankruptcy case. Ambac has significant exposure on its insurance obligation.^{FN5}

After extensive briefing and an evidentiary hearing on February 17, 2010, the court took the matter under submission. It now denies Ambac's motion.

II. LAW

A. Eligibility for Chapter 11, and Jurisdiction of the Court

Ambac alleges that LVMC is ineligible to file a Chapter 11 bankruptcy. With few exceptions, only "a person that may be a debtor under chapter 7" may be a Chapter 11 debtor. 11 U.S.C. § 109(d). Chapter 7 eligibility, in turn, turns on whether the petitioner is a "person" within the meaning of the Bankruptcy Code. A "person" under the Bankruptcy Code is defined in Section 101(41) which states:

The term "person" includes individual, partnership, and corporation, but does not include governmental unit....

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11 U.S.C. § 101(41). As a result, if LVMC is a “governmental unit,” then it cannot be a Chapter 11 debtor, and the court must grant Ambac's motion. *In re Westport Transit District*, 165 B.R. 93, 95 (Bankr.D.Conn.1994); 6 COLLIER ON BANKRUPTCY ¶ 900.02 (Alan Resnick & Henry J. Sommer, eds., 15th ed. rev.2010).

But this determination requires examination of yet another definition, that of “governmental unit.” Section 101(27) defines “governmental unit.” It states:

*3 The term “governmental unit” means United States; State; Commonwealth; District; Territory; municipality; foreign state; department, agency, or instrumentality of the United States ... a State, a Commonwealth, a District, a Territory, a municipality, or a foreign state;....

LVMC is clearly not a State, Commonwealth, District, or Territory. The only included term that might fit is “municipality.” Section 101(40) of the Bankruptcy Code defines “municipality” as follows:

The term “municipality” means political subdivision or public agency or instrumentality of a State.^{FN6}

LVMC is not a political subdivision, such as a county or city. It is not a public agency, such as the Department or the RTC, as it was formed under general nonprofit corporation statutes. At most, it might be an instrumentality of the State of Nevada.

But statutory or caselaw guidance on what constitutes an instrumentality, or even a municipality, is scarce. As noted more than fifteen years ago: “What constitutes a municipality is, despite current Bankruptcy Code language on point, far from clear.” Christopher Smith, *Provisions for Access to Chapter 9 Bankruptcy: Their Flaws and the Inadequacy of Past Reforms*, 14 BANKR.DEV. J. 497, 516 (1998). Clarity has not been achieved in the interim.

B. The Bankruptcy Code and “Municipalities”

[1][2][3][4] Determining the proper scope of Section 101(40)'s use of “instrumentality” raises significant questions of statutory interpretation. The starting point for all statutory interpretation is the presumption that Congress intended the accepted and plain meaning of the words it used.^{FN7} As the Supreme Court has said:

The starting point in discerning congressional intent ...

is the existing statutory text ... and not the predecessor statutes. It is well established that “when the statute's language is plain, the sole function of the courts—at least where the disposition required by the text is not absurd—is to enforce it according to its terms.

Lamie v. United States Trustee, 540 U.S. 526, 534, 124 S.Ct. 1023, 157 L.Ed.2d 1024 (2004) (quoting *Hartford Underwriters Ins. Co. v. Union Planters Bank, N. A.*, 530 U.S. 1, 6, 120 S.Ct. 1942, 147 L.Ed.2d 1 (2000) (internal quotation marks omitted) (in turn quoting *United States v. Ron Pair Enterprises, Inc.*, 489 U.S. 235, 241, 109 S.Ct. 1026, 103 L.Ed.2d 290(1989) (in turn quoting *Caminetti v. United States*, 242 U.S. 470, 485, 37 S.Ct. 192, 61 L.Ed. 442 (1917))). This process typically requires looking “to the ordinary meaning of these terms.” *Rousey v. Jacoway*, 544 U.S. 320, 330, 125 S.Ct. 1561, 161 L.Ed.2d 563 (2005). See also *Pioneer Inv. Servs. Co. v. Brunswick Assoc. Ltd. P'ship*, 507 U.S. 380, 388, 113 S.Ct. 1489, 123 L.Ed.2d 74 (1993) (“Congress intends the words in its enactments to carry ‘their ordinary, contemporary, common meaning.’”) (quoting *Perrin v. United States*, 444 U.S. 37, 42, 100 S.Ct. 311, 62 L.Ed.2d 199 (1979)).

But the nonlegal definition of instrumentality is, unfortunately, anything but ordinary or plain. *Webster's Unabridged Dictionary* defines “instrumentality” variously as “something by which an end is achieved” and “something that serves as an intermediary or agent through which one or more functions of a controlling force are carried out: a part, organ, or subsidiary branch especially of a governing body.”^{FN8} Although undoubtedly accurate definitions, these descriptions are frustratingly slippery to apply in practice, in that they are comprised not of measurable and precise criteria, but rather of reference to function and practice. Even the Supreme Court has given a somewhat vague interpretation of “instrumentality” with respect to the Foreign Sovereign Immunities Act:

*4 A typical government instrumentality, if one can be said to exist, is created by an enabling statute that prescribes the powers and duties of the instrumentality, and specifies that it is to be managed by a board selected by the government in a manner consistent with the enabling law. The instrumentality is typically established as a separate juridical entity, with the powers to hold and sell property and to sue and be sued. Except for appropriations to provide capital or to cover losses, the instrumentality is primarily responsible for its own finances. The instrumentality is run as a distinct economic enterprise; often it is not subject to the same

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budgetary and personnel requirements with which government agencies must comply.

First Nat'l City Bank v. Banco Para El Comercio Exterior de Cuba, 462 U.S. 611, 624, 103 S.Ct. 2591, 77 L.Ed.2d 46 (1983). See also Federal Land Bank v. Bismarck Lumber Co., 314 U.S. 95, 102, 62 S.Ct. 1, 86 L.Ed. 65 (1941) (federal land bank a federal instrumentality given its important governmental function); Rust v. Johnson, 597 F.2d 174, 178 (9th Cir.), cert. denied, 444 U.S. 964 (1979) (Federal National Mortgage Association is federal government instrumentality given its important governmental function).

These differing uses and definitions underscore that no unique or canonical meaning of “instrumentality” exists. An entity or enterprise might be an instrumentality for one purpose, but not for another. Lewis v. United States, 680 F.2d 1239, 1242-43 (9th Cir. 1982) (Federal Reserve Bank an instrumentality for tax purposes but not an instrumentality for purposes of applying the Federal Tort Claims Act); Fed. Reserve Bank v. Metrocentre Imp. Dist. # 1, 657 F.2d 183, 185 n. 2 (8th Cir. 1981) (same).^{FN9} Given this state of affairs, there really is no “plain meaning” of the term “instrumentality”—or, to be somewhat puckish, there are too many plain and accepted meanings—and it thus makes sense to look at the context and background of that term's use in the Bankruptcy Code.

[5] On this score, there is much useful information. When Congress enacted the current 1978 Bankruptcy Code, the components of Chapter 9 eligibility—including the definition of municipality—had been around for more than 50 years. The 1978 Bankruptcy Code, although it tinkered with the definition of municipality, basically adopted the definition of municipality then used in the 1898 Bankruptcy Act. In such cases, the Supreme Court has counseled bankruptcy courts to remember that, when Congress amends existing statutes, it “does not write on a clean slate.” Dewsnup v. Timm, 502 U.S. 410, 417, 112 S.Ct. 773, 116 L.Ed.2d 903 (1992). Courts should thus not “read the Bankruptcy Code to erode past bankruptcy practice absent a clear indication that Congress intended such a departure.” “Travelers Cas. and Sur. Co. of America v. Pacific Gas and Elec. Co., 549 U.S. 443, 454, 127 S.Ct. 1199, 167 L.Ed.2d 178 (2007) (quoting Cohen v. de la Cruz, 523 U.S. 213, 221, 118 S.Ct. 1212, 140 L.Ed.2d 341 (1998) (in turn quoting Pennsylvania Dept. of Public Welfare v. Davenport, 495 U.S. 552, 563, 110 S.Ct. 2126, 109 L.Ed.2d 588 (1990))). This approach indicates that an examination of the historical understanding of Chapter 9

eligibility can help inform the present meaning of “municipality” in Section 101(40).

1. The History of Chapter 9 From a Statutory and Caselaw View

*5 Municipal bankruptcy has been a part of American bankruptcy law since 1934. It arose because of Congress's desire to extend relief to municipalities that States cannot bestow,^{FN10} while simultaneously honoring the constitutional requirements of the Tenth Amendment. A key point of this balance has been the identification of the entities eligible for Chapter 9 relief. One way to better understand the struggle, and its culmination in the words of Section 101(40), is to examine this history.

a. The Statutory Background

First and foremost, Chapter 11 provides federal statutory relief for distressed debtors. It represents a balanced effort to harmonize the often discordant positions of debtors and creditors. As stated by the Supreme Court, reorganization bankruptcy “strikes a balance between a debtor's interest in reorganizing and restructuring its debts and the creditors' interest in maximizing the value of the bankruptcy estate.” Florida Dep't of Revenue v. Piccadilly Cafeterias, Inc., 554 U.S. 33, 128 S.Ct. 2326, 2339, 171 L.Ed.2d 203 (2008) (citing Toibb v. Radloff, 501 U.S. 157, 163, 111 S.Ct. 2197, 115 L.Ed.2d 145 (1991)). No where is that clash more evident, and the balance more difficult to strike, than in Chapter 9 municipal bankruptcy.

(1) Origins in the Depression

The first municipal bankruptcy legislation was enacted in 1934 during the Depression as a temporary measure to assist local governments. Act of May 24, 1934, Pub.L. No. 251, 48 Stat. 798 (1934). This law was captioned “Provisions for the Emergency Temporary Aid of Insolvent Public Debtors and to Preserve the Assets Thereof and for other Related Purposes,” and added Chapter IX to the Bankruptcy Act of 1898. Eligibility for this new statute was limited to:

[a]ny municipality or other political subdivision of any State, including (but not hereby limiting the generality of the foregoing) any county, city, borough, village, parish, town, or township, unincorporated tax or special assessment district, and any school, drainage, irrigation, reclamation, levee, sewer, or paving, sanitary, port, im-

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provement or other districts (hereinafter referred to as a 'taxing district')....

Bankruptcy Act § 80(a), 11 U.S.C. § 303(a) (as enacted in 1934).

Congress was aware of constitutional concerns with municipal bankruptcy, and attempted to address them in the legislation. When challenged the very next year, however, the Supreme Court held, by a 5-4 vote, that the 1934 Act was unconstitutional as an improper interference with the sovereignty of the States. *Ashton v. Cameron County Water Improvement Dist. No. 1*, 298 U.S. 513, 56 S.Ct. 892, 80 L.Ed. 1309 (1936).

Congress responded quickly. It enacted a revised Municipal Bankruptcy Act in 1937, Act of August 17, 1937, Pub.L. No. 302, 50 Stat. 653 (1937).^{FN11} Although this new law changed the list of types of eligible debtors—the full text is reprinted as Appendix 1 given its length—the 1937 Act still required an eligible petitioner to be a “taxing” agency or instrumentality. In short, the revised legislation kept the requirement that municipal debtors had to have the power to tax. That requirement changed in 1946, when Congress revised virtually all of Chapter IX, and made it permanent.

(2) The 1946 Amendments and the Inclusion of Instrumentalities Issuing Industrial Development and Other Revenue Bonds

*6 In 1946, Congress made the municipal bankruptcy provisions permanent, and made some adjustments to the legislation. Act of July 1, 1946, Pub.L. 481, 60 Stat. 409 (1946). One adjustment was a change in the definition of eligibility. Congress removed “taxing” as an adjective in each place in the statute in which it appeared. Again, given its length, the definition is reprinted as Appendix 2 to this opinion.

The purpose of this change was to accommodate the type of financing device at issue in this case—the revenue bond. As explained in the House and Senate Reports that accompanied H.R. 6682 (the bill that became the 1946 Act):

The existing act does not adequately cover what is known as revenue bonds. These are bonds issued by a public agency which are not payable out of taxes but are payable solely from the revenues received from the operation of a revenue-producing public utility or prop-

erty. When the existing act was enacted [in 1937], revenue bonds were not an important factor in municipal financing. Since that time, however, there has been a great development in revenue bond financing and such bonds are now issued by municipalities and other public agencies for many other purposes, such as housing, bridges, tunnels, airports, and similar enterprises. Moreover, the development of this type of financing has brought into existence a new type of municipality known as an authority. In some instances they are called commissions or districts, but essentially they are all of the same character that is, a public agency authorized to construct or acquire a revenue-producing utility and to issue bonds for such purpose payable solely out of the revenues derived from the utility. They possess no power of taxation and were designed as a means of financing public improvements without resorting to the taxing power. The existing law does not apply to this type of municipality.

H.R. 6682 amends the existing statute so as to make it applicable to any type of revenue bond issued by a city, town, county, and so forth, and also to make the act applicable to “authorities.” The extension of the act along these lines is singularly appropriate because the revenue bonds issued by municipalities or authorities are for the purpose of financing revenue-producing enterprises rather than governmental functions. *They are essentially business enterprises.* The investor purchases these bonds relying upon the ability of the municipality to operate such business enterprises at a profit. Obviously these businesses are subject to the same hazards as other businesses financed by private capital. That fact is realized by the investor when he purchases such bonds and he does not depend upon the taxing power of the municipality to meet the principle and interest. Such bonds today enjoy a very wide market.

H.R.REP. NO. 2246, 79th Cong., 2d Sess. 2-3 (1946); S.REP. NO. 1633, 79th Cong., 2d Sess. 2 (1946) (emphasis supplied).

This explicit recognition of revenue bonds is instructive. Reacting to trends in municipal finance which created public entities that did not have taxing powers, Congress kept the basic framework of the definition intact, and just removed the requirement that the entity have the power to tax. To the extent that such entities issued bonds, they would be municipalities for purposes of the Bankruptcy Act.^{FN12}

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*7 This structure and purpose created a negative inference that entities such as LVMC were also to be considered municipalities; otherwise, the legislation could have been easily extended to the entities to whom the public financing was lent, or from whom project revenues were to be received.

The debt to be restructured for the newly-included entities was unlike other debt previously covered by Chapter IX. As recognized by the House and Senate Reports: "The extension of the act along these lines is singularly appropriate because the revenue bonds issued by municipalities or authorities are for the purpose of financing revenue-producing enterprises rather than governmental functions. *They are essentially business enterprises.*" *Id.* (emphasis supplied). And as private business enterprises, they were subject to relief under chapters other than Chapter IX. As summarized by the 1973 Bankruptcy Commission Report: "As the result of several amendments, counties and instrumentalities financed by revenue bonds were added to the list of eligible petitioners." REPORT OF THE COMMISSION ON THE BANKRUPTCY LAWS OF THE UNITED STATES, H.R. DOC. NO. .. 93-137, 93d. Cong., 1st Sess., Pt. I, at 273 (1973).

(3) The 1976 Amendments

Congress did not change the wording of the eligibility requirements for Chapter IX until the City of New York fiscal crisis in the early 1970s. After that crisis, Congress amended the definition of municipality to something more akin to the current Section 101(40). Act of April 8, 1976, Pub.L. 94-260, 90 Stat. 315. In particular, Congress amended Section 81 of the Bankruptcy Act to read: "(8) 'petitioner' means agency, instrumentality, or subdivision which has filed a petition under this chapter." Bankruptcy Act § 81(8), 11 U.S.C. § 401(8) (as amended in 1976).

This change greatly reduced the length of the definition, but no loss in coverage was intended. As indicated in the House Report accompanying the bill that became the 1976 Act, the change "defines petitioner for convenience only. No substantive or limiting result is intended." H.R.REP. NO. 94-686, at 16 (1975). The Conference Report confirmed that the text "adopt[ed] the House language." H.R.REP. NO. 94-938, at 15 (1976).

Industrial development bonds of the type involved in this case did not escape attention. In revising the Chapter IX definition of claims, Congress sought to ensure that revenue bond claims would not be claims in Chapter IX cases.

As stated in the Conference Report:

Municipalities are authorized ... to issue tax-exempt industrial development revenue bonds to provide for the financing of certain projects for *privately owned companies* The municipality merely acts as the vehicle to enable the bonds to be issued on a tax-exempt basis. It is not the intent of the Committee of Conference to include these industrial development bonds in a chapter IX case.

H.R.REP. NO. 94-938 at 15 (emphasis supplied).

*8 Although, these changes would affect entities such as the Department, not LVMC. But they do show Congress's sensitivity to both the entity issuing bonds, and the entity obligated to pay back the bond proceeds.^{FNI13}

(4) Subsequent Amendments

Since 1976, Congress has done little to change the definition of eligibility for municipal bankruptcy relief. Although the 1978 recodification changed the designation of the chapters from Roman numerals to Arabic ones, changed "petitioner" to "municipality," and changed the placement of the definition of municipality, the substance of the definition remained the same. Section 101(40) states that a " 'municipality' means political subdivision or public agency or instrumentality of a State." Given the closeness in time to the 1976 revisions, Congress believed that "[t]he need for substantive revision this year is not great, and H.R. 8200 carries over substantially intact many of the reforms adopted last year." H.R.REP. NO. 95-595, at 263 (1977). As stated later in the *Report*:

The definition is adapted from the terms used in the chapter IX (municipal bankruptcy) amendment to the Bankruptcy Act enacted last year (Pub.L.94-260). That amendment spoke in terms of "political subdivision or public agency or instrumentality of a State". Bankruptcy Act § 84. The term municipality is defined by those three terms for convenience.

Id. at 312-13. See also S.REP. NO. 95-989, at 9 (1978) ("Since [1976], there have been no developments in municipal arrangement proceedings to require any new revision of the law. Thus, the bill tracks the provisions of Public Law 94-260 with stylistic changes to conform to the title.").

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The remarks on the final bill by the floor managers ^{FN14} confirm the role of industrial revenue bonds. As was noted by the floor managers:

The [industrial development] bonds are sold on the basis of the credit of the company on whose behalf they are issued,.... The municipality merely acts as the vehicle to enable the bonds to be issued on a tax-exempt basis. Claims that arise by virtue of these bonds are not among the claims defined by this paragraph *and amounts owed by private companies to the holders of industrial development revenue bonds are not to be included among the assets of the municipality that would be affected by the plan.*

124 CONG. REC. 32,393 (1978) (remarks of Rep. Edwards) (emphasis added); *id.* at 33,992 (remarks of Sen. DeConcini) (emphasis added).

After the 1978 codification, there was significant concern about how Chapter 9 worked in practice. In particular there was concern over how to treat industrial revenue bonds in legitimate Chapter 9 cases. To address this issue, in 1988 Congress added Section 928 to the Bankruptcy Code. That section reads:

(a) Notwithstanding section 552(a) of this title and subject to subsection (b) of this section, special revenues acquired by the debtor after the commencement of the case shall remain subject to any lien resulting from any security agreement entered into by the debtor before the commencement of the case.

*9 (b) Any such lien on special revenues, other than municipal betterment assessments, derived from a project or system shall be subject to the necessary operating expenses of such project or system, as the case may be.

Municipal Bankruptcy Amendments, Pub.L. No. 100-597, § 8 (1988) (codified at 11 U.S.C. § 928). The purpose of this provision was to continue the isolation of industrial revenue bond financing from general municipal bond financing. As stated in *Collier*, “[i]n general, its effect is to prevent special revenues that secure an issue of revenue bonds from being diverted to be available for the municipality’s general expenses or obligations.” 6 COLLIER ON BANKRUPTCY, *supra*, at ¶ 928.01.

Congress also acknowledged the separation between in-

dustrial revenue bonds and general obligation bonds:

At the same time the municipality approves financing through a revenue bond project or program, however, it has made the assumption that the project or program will generate adequate revenues to repay the bondholders and operate the project or program without any general financial obligation on the part of the municipality. Thus, unlike [general obligation] bonds, the general taxpayers are usually not committed to repaying the bonds or funding operational deficits through general tax revenues.

S.REP. NO. 100-506, at 4 (1988). *See also* H.R. REP. 100-1011, at 4 (1988) (“Special revenue bonds are issued so that if the asset financed fails, repayment will not come out of general treasury funds—meaning the taxpayer will not have to foot the bill.”)

At the same time, however, Congress understood and protected the creditors of the special entity borrowing the money raised by the bond financing (and upon whose success the bonds depend). Section 928(b) essentially subordinates any lien held by bondholders to “necessary operating expenses of such project or system....” As stated again in *Collier*:

The general purpose of this approach is to permit the continued operation or functioning of the system, project, or function that was financed by the revenue bonds. Without such continued operation, there is not likely to be a continued source of funds from which to service the bonds. The pledged revenues would not be permitted to be used for any other governmental purpose, but would be used to pay operating expenses to facilitate a workout and successful confirmation of an adjustment plan.

6 COLLIER ON BANKRUPTCY, *supra*, at ¶ 928.03.

Congress passed the final set of amendments relevant to this case in 1994. Although these amendments did not change the definition of municipality in Section 101(40), they did indicate a narrowing of eligibility. Before the 1994 amendments, States merely had to generally authorize a municipality’s filing. Section 402 of the 1994 Act, however, amended Section 109(c)(2) of the Code by striking “generally authorized” and inserting “specifically authorized, in its capacity as a municipality or by name.” Bankruptcy Reform Act of 1994, Pub.L. No. 103-394, § 402 (1994).

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*10 Nevada, along with a majority of States, has not specifically authorized its municipalities to file Chapter 9 bankruptcy. See Daniel J. Freyberg, *Municipal Bankruptcy and Express State Authorization to Be a Chapter 9 Debtor: Current State Approaches to Municipal Insolvency-and What Will States Do Now?*, 23 OHIO N.U. L.REV. 1001, 1008-09 (1997) (finding 14 States that had specifically authorized municipalities to file Chapter 9); NATIONAL BANKRUPTCY REVIEW COMM'N, BANKRUPTCY: THE NEXT TWENTY YEARS-NATIONAL BANKRUPTCY REVIEW COMMISSION FINAL REPORT, OCTOBER 20,1997, at 988 n. 2431 (1997) (finding 12 States that had specifically authorized municipalities to file Chapter 9). To the contrary, Nevada has enacted a elaborate and complete scheme of regulation for local municipalities that does not grant municipalities the right to file Chapter 9 bankruptcy. NEV.REV.STAT. §§ 354.655-.725.

(5) Summary of Legislative Review

This review of the legislation, suggested by *Travelers, Davenport*, and *de la Cruz* in order to find the pre-1978 understanding of municipality, suggests that Chapter 9's origins looked initially and with great weight into the ability of the entity or enterprise to tax or levy assessments. It is this ability that attracted the disapproval of the Supreme Court with respect to Congress's initial efforts to extend federal bankruptcy relief to State entities. Put simply, the Court saw Tenth Amendment concerns in a federal procedure that could force State and local governments to tax their citizens without their direct consent.

But starting in 1946, Congress moved away from a test that centered on taxing powers. Recognizing the rise of new forms of municipal finance, the 1946 amendments opened up then-Chapter IX to agencies and other departments of local government that, while devoid of the power to tax, had the ability to contract and to issue debt. This recognition extended through the 1976 amendments. Even though these amendments came thirty years later, they also acknowledged that private companies can facilitate municipalities' missions without themselves becoming municipalities. As noted in the debates leading up to the 1976 amendments, "[t]hese transactions should really be handled outside the Chapter IX case." 121 CONG. REC. 39,412 (1975) (remarks of Rep. Edwards).

The 1988 amendments cemented this view. Congress added Section 928 to continue the separate treatment of

revenues from special revenue bond projects and revenues arising from taxation. This structuring recognizes that entities which facilitate public functions do not raise the historic concerns that have animated the various definitions related to Chapter 9 eligibility. Congress has essentially assumed that, while such entities are affiliated with municipalities, they are not municipalities themselves.

b. Caselaw Interpretations of the Bankruptcy Code's Definition of "Municipality"

Along with the legislative developments, caselaw similarly evolved to recognize that entities created to facilitate public financing of infrastructure projects might not themselves be municipalities. One of the first cases to examine the modern definition of "municipality" was *Ex parte York County Natural Gas Authority*, 238 F.Supp. 964 (W.D.S.C.1965), modified on other grounds by, *Mozingo v. York County Natural Gas Authority*, 362 F.2d 78 (4th Cir.1965), cert. denied, 383 U.S. 970, 86 S.Ct. 1277, 16 L.Ed.2d 310 (1966). There, the court had before it the 1946 definition of "municipality." The entity before it had been created by the South Carolina Legislature in 1954. The authorizing legislation stated:

*11 There is hereby created a body corporate and politic of perpetual succession to be known as the York County Natural Gas Authority (hereinafter sometimes referred to as the authority). It shall be the function of the authority to purchase, lease, acquire, build, construct, maintain and operate natural gas distribution systems within the service area....

York County, 238 F.Supp. at 966 (quoting Section 1 of the South Carolina General Assembly's Act 959 of 1954, as subsequently amended). The same legislation gave the gas authority a full set of rights, powers and duties with respect to its management, operations and business affairs, and identified the authority as a "body corporate and politic."

The legislation also gave the gas authority the power to issue revenue bonds, but such bonds had to be non-recourse as to the State and as to any of the other public entities served by the gas authority. *Id.* at 966-67. After its formation, the gas authority had financial trouble, engaged in refinancing efforts, and ultimately filed a petition under Chapter IX.

Its status as an eligible Chapter IX debtor was questioned. Given the scope of the legislative grant creating it, how-

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ever, the court held that the gas authority was a “public agency” as referred to in Chapter IX’s definition of “municipality.” In so holding, the court stated that “[t]he legal test between a private or public authority or agency is whether the authority or agency is subject to control by public authority, state or municipal.” *Id.* at 976 & n. 11 (quoting *Kerr v. Enoch Pratt Free Library of Baltimore*, 54 F.Supp. 514 (D.C.Md.1944)).^{FNI5} Without much discussion, *York County* apparently considered it self-evident that the gas authority qualified as an agency or authority within the meaning of the statute.

The next case to examine the definition of municipality in any detail was *In re North and South Shenango Joint Municipal Authority*, 14 B.R. 414 (Bankr.W.D.Pa.1981), *rev’d on other grounds*, 80 B.R. 57 (W.D.Pa.1982).^{FNI6} In *Shenango*, the subject entity was a municipal authority established to construct and operate a sewer system on behalf of two Pennsylvania townships. The bankruptcy court held that the entity was a “municipality” under the 1978 Bankruptcy Code essentially for three reasons: (1) the entity was “incorporated” under Pennsylvania’s Municipality Authorities Act, *id.* at 415; (2) state caselaw already had classified municipal authorities created under this act as public agencies and instrumentalities of the State, *id.* at 418; and (3) the entity had governmental powers conferred upon it by statute, including the power of eminent domain, and the power to assess sewer and water main construction costs, *id.* at 415-16. *Shenango* thus not only looked to the level of State control over the entity’s organization and operations, but also the intent of the State that created it.

The characterization used by the State that created the entity at issue was also a factor in *In re Pleasant View Utility Dist. of Cheatham County*, 24 B.R. 632 (Bankr.M.D.Tenn.1982). There, a county had created the debtor utility district to provide water services. The district had the authority to issue revenue bonds, and did so by resolution of its governing board of commissioners. *Id.* at 634.

*12 Unlike *York County* and, to a lesser extent, *Shenango*, the case does not give any indication whether there was any State control over the district’s operations or management. With virtually no analysis, *Pleasant View* concluded that the district was a municipality for bankruptcy purposes:

The parties do not seriously dispute that the District is a municipality as defined by the Bankruptcy Code. 11

U.S.C.A. § 101(29) (West 1979) defines municipality as a ‘political subdivision or public agency or instrumentality of a State.’ This definition clearly encompasses a utility district such as the debtor, which [Tennessee law] classifies as a municipality or public corporation.^{FNI7}

Pleasant View, 24 B.R. at 635. The court also noted that other provisions of the same chapter empowered such districts to make assessments, condemn property, and operate the utilities controlled by the district for the public benefit. *Id.*

The next series of cases examining the definition of “municipality” focused on *York County*’s concept of control. In *In re Greene County Hosp.*, 59 B.R. 388 (S.D.Miss.1986), for example, a community hospital filed for Chapter 9 bankruptcy. The bankruptcy court determined that the hospital was eligible to be a debtor under Chapter 9, and the district court affirmed.

According to the district court, the bankruptcy court had correctly determined that the hospital was a public agency, and thus a municipality. The district court adopted *York County*’s definition of public agency: “The legal test between a private or public authority or agency is whether the authority or agency is subject to control by public authority, state or municipal.” *Greene County Hospital*, 59 B.R. at 389 (citing *York County*, 238 F.Supp. at 976). The district court did not consider other aspects of the hospital’s nature, purpose or governance, but rather affirmed based on the amount of public control.

The district court found that even though community hospitals in Mississippi controlled their own day-to-day hospital operations, the county board of supervisors controlled issues relating to property management. According to the district court, this was enough to make the hospital a public agency of Mississippi, and, therefore, a municipality under the Bankruptcy Code. *Id.* at 390.

In reaching this conclusion, the district court seemed to use flawed reasoning: while it is true that the complete absence of public control likely would establish that an entity is not a municipality, the converse is not necessarily true. A limited measure of public control, regulation or oversight simply does not, by itself, make an entity a public agency. Otherwise, heavily regulated industries, such as casinos and taxi cabs, would be municipalities.

The absence of control was also an issue in *In re Ellicott*

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School Bldg. Authority, 150 B.R. 261 (Bankr.D.Colo.1992). There, a school building authority was created under Colorado's nonprofit corporation act for the purpose of acquiring land and constructing a school. The authority had the power to issue revenue bonds to finance the purchase and did so. The authority's revenues consisted of rent paid by the school district for the use of the school, and this rental stream was the authority's sole authorized source of revenue. The authority had no power to levy taxes or make assessments.^{FNI8}

*13 The authority had been structured as a nonprofit corporation to meet the requirements of IRS Revenue Ruling 63-20, "in order to qualify as a governmental or quasi-governmental issuer whose obligation may then qualify as tax exempt under ... the Tax Code...." 150 B.R. at 263. Based on the contents of the disclosure statement related to the authority's revenue bonds, and the court's finding that "no governmental entity exercises any right of control" over the authority, the court concluded that the authority was not a municipality within the meaning of the Bankruptcy Code.

In reaching this holding, the court relied on the control test set forth in *York County* and *Greene County Hospital*. Important for this case, *Ellicott* is instructive in the treatment given to an issuer of tax exempt municipal bonds; contrary to the thrust and purpose of the 1946 Amendments to the definition of municipality, the court held that the authority at issue—even though it issued tax-exempt bonds—could not qualify as a municipality. Here, of course, there are at least two major distinctions: first, the Director, and not LVMC, issued the Bonds, and second, the State of Nevada has retained the ability to control significant parts of LVMC's governance and operations.

The designations used by local authorities were again at issue in *In re Sullivan County Regional Refuse Disposal Dist.*, 165 B.R. 60 (Bankr.D.N.H.1994). There, under State and federal legislation enacted to encourage cities to band together to achieve the environmental and economic benefits associated with large-scale waste-disposal operations, the debtor had been set up as a "privatization" joint venture. Among the members of the joint venture were towns, cities, and a private company that owned and operated a waste-to-energy rubbish incinerator. The district agreed to pay the private incinerator owner/operator certain guaranteed minimum amounts for the use of the incinerator, and the district in turn collected tipping fees from its customers.

In theory, the district had the power to assess member cities for any shortfall in revenue, but in practice were unable to actually make any assessments because the member cities voted to block such assessments. *Id.* at 66. *Sullivan County's* analysis of whether the district is a municipality is somewhat cursory. Essentially, because State law described the district as a "body politic and corporate," the court concluded that the district was a municipality. *Id.* The court further stated: "[i]t is beyond dispute that [the district] is a political subdivision of the state in implementing federally mandated solid waste laws." *Id.* at 73.

While *Sullivan County* did not make any attempt to parse Section 101(40)'s terms "political subdivision," "public agency" or "instrumentality of a state," the case is instructive in one respect: it gave significant weight to how State law classified and treated the district.

*14 Both control and local designation came together in *In re Westport Transit District*, 165 B.R. 93 (Bankr.D.Conn.1994). There, the town of Westport created a transit district in order to provide public transportation services to its citizens. State enabling statutes identified such districts as bodies "corporate and politic" and provided for such districts to assume a number of powers and duties within their boundaries otherwise held by the State's department of transportation. These included setting fares, regulating transit systems, and using revenues to subsidize privately-owned transit companies. *Id.* at 95-96.

In addition, State authority allowed the district to have the power of eminent domain and the ability to issue bonds. When the district filed a Chapter 9, it was challenged on the grounds, among others, that the district was not a municipality. The bankruptcy court disagreed.

The objecting party argued that the district was an instrumentality of the town of Westport, and that the Bankruptcy Code definition of municipality required the district instead to be an instrumentality of the State. *Westport* rejected this argument, citing *York County* (which held that public agencies are subject to governmental control, "state or municipal"). It also looked to the significant amounts of governmental authority the district possessed, such as eminent domain, and the power to choose between public or private solutions to the transit problems with its geographical area. Combined with the State designation, the court found this to be a sufficient basis to hold that the district was a municipality within the mean-

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ing of the Bankruptcy Code.

Perhaps the best-known case addressing the definition of municipality is *In re County of Orange*, 183 B.R. 594 (Bankr.C.D.Cal.1995). In *County of Orange*, the county treasurer had created a commingled investment pool of government funds received from different governmental entities. The treasurer then made a series of disastrous financial decisions which drained the pool of much of its capital. When the county filed for Chapter 9 relief, this separate investment pool, referred to by the court as OCIP, also filed a Chapter 9 petition. OCIP's status as a municipality was challenged, and the bankruptcy court agreed it was not a municipality.

In reaching its conclusion, *County of Orange* methodically parsed the meaning of the term "municipality," and its history. It made several findings on its way to holding that OCIP was not a municipality. First, it held that OCIP was not a "political subdivision" because, as the court found, "political subdivision" was a phrase reserved for public entities bestowed with sovereign powers, such as the power of eminent domain, the police power, or the power to assess and levy taxes. Second, the court held that OCIP was not a "public agency" because the court held that this phrase was reserved for publically-controlled entities created to operate revenue-producing enterprises and/or to finance revenue-producing enterprises through the use of government-issued bonds. Finally, the court held that OCIP was not an "instrumentality of a State," because the court held that this phrase was reserved for specific kinds of improvement districts of which OCIP was not one.

*15 According to *County of Orange*, these meanings could be derived from line item descriptions of the specific types of entities qualified to file municipal bankruptcy contained in the predecessor statute to Chapter 9. See *County of Orange*, 183 B.R. at 600-603 (arguing that Section 81(7) of the 1898 Act defined political subdivisions, Section 81(6) defined public agencies and Sections 81(1)-(5) defined instrumentalities).

County of Orange has been criticized for being overly-precise in creating these definitions of the terms "political subdivision," "public agency" and "instrumentality of a State."

The suggestion that the three categories "political subdivision," "public agency" and "instrumentality of a State" should be defined exclusively by the categories

of agencies and instrumentalities set forth in Section 81 of the 1937 Act is misplaced because the Bankruptcy Code definition of municipality is strikingly dissimilar to the language of Section 81 of the 1937 Act; the suggestion fails to give effect to Congress's intention to broaden the definition of 'municipality.' "

2 COLLIER ON BANKRUPTCY, *supra*, at ¶ 109.04[3][a].

Put simply, although Congress stated that "[n]o substantive or limiting result is intended," H.R.REP. NO. 94-686, at 16 (1975), the 1976 elimination of the lengthy description of the various types of entities and the switch to generic descriptions was not completely without effect. Given the subtle and constant change in municipal organization and finance, Congress clearly did not want to limit its definitions in a way that restricted eligibility. To give effect to Congress's intent to "broaden the applicability of Chapter IX as much as possible," *id.* at 20, courts cannot be shackled to difficult-to-find and elaborate descriptions of mid-20th Century municipal organization. That conclusion, however, does not answer the central question posed here: what is an instrumentality for purposes of Section 101(40)? Answering this question requires a further synthesis of the history and interpretation of the definition.

2. Synthesizing the Components of an Instrumentality

The examination of the history of the Bankruptcy Code's use of municipality and instrumentality show three distinct threads. The first thread focuses on whether the entity has any of the powers typically associated with sovereignty, such as eminent domain, the taxing power or sovereign immunity. *E.g.*, *Westport Transit District*, 165 B.R. at 95-96; *Shenango*, 80 B.R. at 415-16.

If those powers are absent or only weakly present, then courts examine whether the entity has a public purpose. If so, the level of control exerted by the State (or its agreed agents) on the entity's activities in furtherance of that purpose is relevant; the more control over day-to-day activities, the more likely the entity is an instrumentality under Section 101(40). *E.g.*, *Ellicott School Bldg. Authority*, 150 B.R. at 263; *Greene County Hospital*, 59 B.R. at 389; *York County*, 238 F.Supp. at 976 & n .11.

*16 The final thread analyzes the effect of the State's own designation and treatment of the entity. *E.g.*, *County of Orange*, 183 B.R. at 600-03; *Sullivan County*, 165 B.R. at

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66; *Pleasant View*, 24 B.R. at 634.

a. *Components of a Federal Definition of "Municipality"*

[6] As indicated above, the extent to which these threads must be interwoven to constitute a "municipality" under the Bankruptcy Code starts with an examination of the function and powers of the entity. Does the entity have traditional governmental attributes or does it engage in traditional governmental functions? If it does, it likely is a municipality because it is probably a political subdivision or State agency, separate components of the definition of municipality. See *County of Orange*, 183 B.R. at 600-03; *Shenango*, 80 B.R. at 415-16. If not, then the inquiry moves to whether the entity is an instrumentality, and that inquiry turns to the level of State control.

[7][8] If the entity's purpose or attributes reflect a public purpose—that is, they reflect goals and activities which augment the State's provision of some public function—the inquiry next focuses on the extent to which the State controls the implementation of those functions and attributes. This inquiry is necessary because many entities have public functions—the Red Cross and other charities come to mind—but are not instrumentalities of the State because of the lack of any State process to control their activities. If there is State control coupled with public function, then the nature and extent of that control determine whether the entity is an instrumentality. In this regard, the type of control is critical. If the control retained or exercised is necessary or designed to allow the State to manage its finances or its fisc—the traditional concerns of Chapter 9—then the entity is an instrumentality. If the control, however, is more akin to oversight or regulation, then the entity is not an instrumentality. See *Ellicott School Bldg. Authority*, 150 B.R. at 263; *Greene County Hospital*, 59 B.R. at 389.

[9] Finally, some deference is given to the State's categorization of the entity. While not determinative, this thread reflects the policy of not interfering with a State's ability to select the form of financial assistance its agencies and departments may use. Given that the 1994 amendments required States to authorize specifically a Chapter 9 filing, it is apparent that Congress desired States to have great leeway in ordering these functions. In many cases, the State's classification will be determinative not because of the label applied, but because that label carries with it, under State law, the powers and functions that are essential to a municipality. See *County of Orange*, 183 B.R. at 600-03.

Each of these inquiries is essentially factual. Given the myriad ways in which the State can express and disburse its power, what may be sufficient control in one context is insufficient in another. Often, however, the design is made explicit through the State's own categorization of the entity.

b. *LVMC's Representation That It Is An Instrumentality*

*17 [10] Ambac contends, however, that LVMC's execution of the Tax Certificate essentially overrides this analysis. Ambac's main argument rests on the undisputed fact that LVMC represented in the bond offering that it was an instrumentality of the State of Nevada and that it was under control of the Governor of Nevada. Since "instrumentality" is part of the definition of "municipality" in Section 101(40), it believes this statement essentially settles the matter.

[11] The fatal problem with Ambac's argument is that the Supreme Court has rejected its basic premise—that a word used in one federal statute necessarily has the same meaning in another federal statute. In *United States v. Reorganized CF & I Fabricators of Utah, Inc.*, 518 U.S. 213, 116 S.Ct. 2106, 135 L.Ed.2d 506 (1996), for example, the issue was whether an exaction denominated a tax by Congress in Section 4971 of the Tax Code was an "excise tax" for purposes of priority under Section 507(a)(7)(E) of the Bankruptcy Code. In rejecting that the exaction was even a tax, and hence not an excise tax, the Court used its own historical definition of "tax" developed for purposes of priority claims under both the 1898 Act and the 1978 Code. Its analysis of why it did not simply adopt Congress's label is worth quoting at length:

Here and there in the Bankruptcy Code Congress has included specific directions that establish the significance for bankruptcy law of a term used elsewhere in the federal statutes. Some bankruptcy provisions deal specifically with subjects as identified by terms defined outside the Bankruptcy Code.... Other bankruptcy provisions directly adopt definitions contained in other statutes;.... Not surprisingly, there are places where the Bankruptcy Code makes referential use of the Internal Revenue Code,....

It is significant, therefore, that Congress included no such reference in § 507(a)(7)(E), even though the Bankruptcy Code itself provides no definition of "excise," "tax," or "excise tax." This absence of any explicit con-

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necter between §§ 507(a)(7)(E) and 4971 is all the more revealing in light of the ... history of interpretive practice in determining whether a “tax” so called in the statute creating it is also a “tax” (as distinct from a debt or penalty) for the purpose of setting the priority of a claim under the bankruptcy laws.

Reorganized CF & I Fabricators, 518 U.S. at 219-20.

The Court expanded on the meaning of a lack of a specific cross-reference later in its opinion:

Congress could, of course, have intended a different interpretive method for reading terms used in the Bankruptcy Code it created in 1978. But if it had so intended we would expect some statutory indication, *see Midlantic Nat. Bank v. New Jersey Dept. of Environmental Protection*, 474 U.S. 494, 501, 106 S.Ct. 755, 759-760, 88 L.Ed.2d 859 (1986), whereas the most obvious statutory indicator is very much to the contrary: in the specific instances noted before, it would have been redundant for Congress to refer specifically to Internal Revenue Code definitions of given terms if such cross-identity were to be assumed or presumed, as a matter of interpretive course.

*18 Reorganized CF & I Fabricators, 518 U.S. at 221-22.

This analysis acknowledges two points: that in a perfect world identical words would have identical meanings wherever and whenever used; and that we do not live in a perfect world. For purposes of statutory analysis, it is not uncommon for the same word or phrase to have different meanings in different codes; the scope of the word “lease,” for example, is particularly slippery in the tax code,^{FN12} and in any event has different nuances than “lease” in the Uniform Commercial Code, U.C.C. § 2A-103(1)(j), or under general accounting principles. *See* FIN. ACCOUNTING STANDARDS BOARD, Statement of Fin. Accounting Standard No. 13 (1976); INT’L ACCOUNTING STANDARDS BOARD, Int’l Accounting Standard 17 (2009). “Security interest” is another example of the same words having different meanings in different codes. *Compare* 26 U.S.C. § 6323(h)(1) with 11 U.S.C. § 101(51) with U.C.C. § 1-201(37).

Against this background, it is critical to note that LVMC did not make its representation in connection with an acknowledgment that it was ineligible for Chapter 11. Rather, LVMC made this statement in connection with its efforts to ensure that interest on the Bonds would be free

from federal taxation—indeed, the Bond offering itself told investors that LVMC could not waive bankruptcy protection.^{FN20} The different context underscores why this court cannot find LVMC is an instrumentality under the Bankruptcy Code simply because it asserted it was one under the Tax Code. While the various definitions may be similar, they are not the same, thus necessitating a separate and full inquiry as to the content of the term “instrumentality” in the Bankruptcy Code.^{FN21}

But while the argument regarding identity of meaning fails, there is some merit in Ambac's control argument. As noted above, control is an essential element in determining whether an entity is an instrumentality under Section 101(40). Ambac contends that LVMC's representation that the State of Nevada had control over its activities is a factual statement that satisfies the elements of control required in any Section 101(40) analysis.

Ambac's argument thus resolves into an assertion that the level of “control” which leads to a finding of an instrumentality under tax law is the same level of “control” Section 101(40) requires for its use of “instrumentality.” There is some precedent for this analogy; an entity's attributes for tax purposes can often be quite relevant when determining bankruptcy eligibility. *See, e.g., In re Sung Soo Rim Irrevocable Intervivos Trust*, 177 B.R. 673, 677-79 (Bankr.C.D.Cal.1995) (using federal tax law on spendthrift and business trusts to assess eligibility under § 109).

To assess this claim, however, the court must examine what “control” was necessary for the tax analysis, and whether the components of that control are consistent with the Bankruptcy Code's purposes. Only after examining these two aspects of control can the two uses—one tax, the other bankruptcy—be compared.

c. The Relevance of LVMC's Tax Status as an “Instrumentality”

*19 LVMC's instrumentality status was critical to the Director's issuance of the Bonds. That status allowed the Director to offer the Bonds on the basis that interest payments would be free of federal tax, which in turn lowered LVMC's cost of expanding and running the monorail. But one can ask why that was so: the Director issued the Bonds, not LVMC, so why was LVMC's status critical if the Bonds were those of the Director, clearly a State agency? The answer lies in assumptions made generally by the IRS. For transactions such as the one at issue here, the IRS views a loan to an instrumentality as a loan to the

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governmental unit on behalf of the instrumentality. Rev. Proc. 82-26, § 3.041(a), 1982-1 C.B. 476; I.R.S. Priv. Ltr. Rul. 96-24-013 (March 15, 1996).

In this respect, tax law favors functional over literal categorizations; it looks to the status of the ultimate borrower-LVMC-and not of the legal issuer of the Bonds-the Director. Under this analysis, if LVMC is an instrumentality under the tax considerations, then the Financing Agreement to LVMC is treated as a loan to a governmental unit, and LVMC's payment of interest on that loan is accordingly free of federal tax to the holders of the Bonds. In short, the regulations leapfrog testing the nominal obligor on the Bonds in favor of imposing a test on the ultimate obligor for the project.

This policy may promote collection of federal taxes, but it has little relevancy to the federal policy concerns behind Chapter 9 availability. As shown by the legislative history of Chapter 9 eligibility, Congress has been quite solicitous of States' protection of their revenues and their ability to control how they perform their essential public functions. To the extent that such integral government operations have been held or exercised by entities filing federal bankruptcy, courts have also been solicitous in classifying the entities involved as municipalities.

[12] Here, however, the State of Nevada's involvement falls in a somewhat unexplored area between essential public function and State oversight. As a result, while the tax authorities reviewing the appropriate level of control necessary for the Bonds' tax treatment are relevant, they are not controlling in any sense for the simple reason that they incorporate assumptions that do not carry over well into Section 101(40). Put another way, if an entity is not an instrumentality for tax reasons, it is quite likely it will not be an instrumentality for bankruptcy purposes; the obverse, however, may not be true. The level of control necessary for federal municipality status, since it focuses on the exercise of traditional municipal powers, is generally higher than that required for tax exempt status. But tax analysis can inform the decision of the necessary level of control, and thus the court will canvass Ambac's tax authorities.

(1) Revenue Ruling 57-128

There is a long and full history of what is required for interest on revenue bonds to be tax exempt. Most agree that the inquiry starts with a 1957 Internal Revenue Service ("IRS") Revenue Ruling. In Revenue Ruling 57-128,

1957-1 C.B. 311, a voluntary unincorporated organization formed by State insurance officials to promote uniformity in legislation affecting insurance sought exemption from having to pay federal unemployment tax on its employees. The association's membership consisted of commissioners, directors, superintendents, or other officials who by law were charged with the responsibility of supervising the insurance business within their respective States. The organization's officers were selected from its members.

*20 The IRS, in finding that such an organization was an instrumentality, looked at the following six factors:

In cases involving the status of an organization as an instrumentality of one or more states or political subdivisions, the following factors are taken into consideration: (1) whether it is used for a governmental purpose and performs a governmental function; (2) whether performance of its function is on behalf of one or more states or political subdivisions; (3) whether there are any private interests involved, or whether the states or political subdivisions involved have the powers and interests of an owner; (4) whether control and supervision of the organization is vested in public authority or authorities; (5) if express or implied statutory or other authority is necessary for the creation and/or use of such an instrumentality, and whether such authority exists; and (6) the degree of financial autonomy and the source of its operating expenses.

Rev. Rul. 57-128, 1957-1 C.B. 311, at 3.^{FN22}

Revenue Ruling 57-158 has been applied in a wide array of cases. In Rev. Rul. 65-26, 1965-1 C.B. 444, for example, a municipal league had been formed as a nonprofit corporation. Its purpose was to improve municipal government and the general welfare of the cities in the State in which it was formed. Its members were public officials from the member cities. It published a magazine, conducted conferences and sponsored research and surveys. Its income derived solely from the sale of these products. Given this attenuated connection with government, and the fact that the board members acted as individuals and not as officers of their respective municipalities, the IRS took the position that the entity was not an instrumentality.^{FN23}

In contrast, in Rev. Rule 65-196, three municipal corporations formed an entity to jointly own and operate recreational facilities for their residents. Each municipality ap-

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pointed the members of the governing board; in contrast to Rev. Rul. 65-26, however, the members could not hold any other public office. One of the member municipalities issued the industrial revenue bonds to finance the project, and the three municipalities took title to the project in proportion to their respective populations. Upon dissolution, remaining assets would be distributed to the member municipalities. Given the more direct involvement of the municipalities, from creation to finance to ownership to dissolution, the IRS stated that the entity was an instrumentality. *Id.* See also Rev. Rul. 79-95, 1979-1 C.B. 331 (local transit authority exempt from federal excise tax given its possession of the power of eminent domain and the power to appoint transit police with the same authority as municipal police).

(2) Beyond Revenue Ruling 57-128

The IRS reiterated its criteria, albeit in a slightly different manner, in Rev. Rul. 89-49, 1989-1 C.B. 117. There, a volunteer fire department, organized under a State's nonprofit corporation law, had contracted with several municipalities for fire protection service. It also received donations from affected citizens. It was governed by its own board of trustees, who were not selected by any municipal agency. The question arose as to whether it was an instrumentality of the State, as such status would greatly affect its retirement plan for its firefighter employees. In holding that it was not, the IRS said:

*21 One of the most important factors to be considered in determining whether an organization is an agency or instrumentality of the United States or any state or political subdivision is the degree of control that the federal or state government has over the organization's everyday operations. Other factors include: (1) whether there is specific legislation creating the organization; (2) the source of funds for the organization; (3) the manner in which the organization's trustees or operating board are selected; and (4) whether the applicable governmental unit considers the employees of the organization to be employees of the applicable governmental unit. Although all of the above factors are considered in determining whether an organization is an agency of a government, the mere satisfaction of one or all of the factors is not necessarily determinative.^{FN24}

Here, LVMC's execution of the Tax Certificate undoubtedly relied upon the level of control imposed by the State of Nevada. LVMC must present its annual budget to the Governor, who has the power to veto it. LVMC must ob-

tain the Governor's consent for its fare schedule. The Governor selects its board of directors. LVMC's assets escheat to the State upon its dissolution. Each of these attributes goes directly to the third factor in Rev. Rul. 57-158, "whether there are any private interests involved, or whether the states or political subdivisions involved have the powers and interests of an owner," as well as the fourth factor, "whether control and supervision of the organization is vested in public authority or authorities." Here, the assertion is that the participation in strategic and high level decisions-such as budget and selection of directors-when combined with the residual interest in any assets, is sufficient for control under the tax instrumentality test, and thus should be sufficient for the bankruptcy instrumentality test.

But the tax tests are not rigid; they rely on factors for which the person applying the test must supply the weight to be given. Two of the factors highlighted in Rev. Rul. 89-49 favor non-instrumentality status: there was no specific legislation creating LVMC-it is incorporated under the State's nonprofit corporation law-and its operating funds come from fares paid by the general public, not taxes. These factors were also present in Rev. Rul. 57-128. Moreover, its day-to-day operations are vested in officers not selected by public officials, and it has incurred debt beyond that related to the Bonds. Moreover, as shown by the Trustee's motions with respect to cash collateral, entities other than public entities can and do control its ability to incur and pay day-to-day and strategic expenses. Finally, its uneasy relationship with the RTC, a public agency with eminent domain power, shows that Rev. Rul. 57-158's second factor-"whether performance of its function is on behalf of one or more states or political subdivisions"-is weak, especially when considering that LVMC is treated by other public agencies as a private entity; LVMC must still obtain a business license and franchise to operate from Clark County, just as would any other business.

*22 This uncertainty is, to some extent, to be expected. As noted in 1998, "[t]he instrumentality tests, of course, do not avoid all difficulty or ambiguity." Ellen P. Aprill, *The Integral, the Essential, and the Instrumental: Federal Income Tax Treatment of Governmental Affiliates*, 23 J. CORP. L. 803, 822 (1998).^{FN25} Regardless of treatment under the tax code, however, the instrumentality test under the Bankruptcy Code is separate and independent. And application of federal bankruptcy principles indicates that LVMC is not a municipality under Section 101(40).

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C. LVMC is Not a Municipality Under the Bankruptcy Code

[13] As indicated above, the inquiry under Section 101(40) involves interpretation of three basic sets of characteristics: the extent to which the entity has traditional governmental attributes or engages in traditional governmental functions; the extent to which the State controls the entity's operations, with elements that go to control of the State's finances having more weight than elements that may simply be general regulation; and the extent to which the State itself categorizes the entity as a municipality or instrumentality.

1. Do LVMC's Transportation Goals Constitute Traditional Governmental Functions?

The initial step in determining whether LVMC is a municipality is to examine its functions and operation. No one seriously contends that LVMC is a political subdivision or agency of the State of Nevada. It has no power to tax, no power of eminent domain, and no sovereign immunity. Westport Transit District, 165 B.R. at 95-96; Shenango, 80 B.R. at 415-16. Cf. Washington State Dairy Prods. Comm'n v. United States, 685 F.2d 298 (9th Cir.1982) (because immunity from taxation is based on "respect for state sovereignty," "only entities possessing at least some portion of the state's sovereign powers or performing traditional government functions qualify for [tax] exemption."); Rev. Rul. 79-95, 1979-1 C.B. 331 (local transit authority exempt from federal excise tax given its possession of the power of eminent domain and the power to appoint transit police with the same authority as municipal police). Treas. Reg. § 1.103-1(b) ("The term "political subdivision," for purposes of this section denotes any division of any State or local governmental unit which is a municipal corporation or which has been delegated the right to exercise part of the sovereign power of the unit.").

LVMC is a creature of general nonprofit corporation laws rather than of a specific legislative enactment. This analysis shows that the first thread of the definition of a municipality—that of direct exercise of a public function—is lacking. But this absence does not mean that LVMC is not without a public purpose, a point made by the basis of its exemption from federal tax on its income.^{FN26}

The argument was also raised that regulation and control cannot be factors. The example of taxi companies was used; they provide and assist the public function of trans-

portation, and are under regulation of the most intrusive type. Yet no one seriously considers taxi companies instrumentalities of the State and, so the argument goes, control cannot be a factor. This is not wrong, yet it is not right either. Control, as the cases show, matters. Ellicott School Bldg. Authority, 150 B.R. at 263; Greene County Hospital, 59 B.R. at 389; York County, 238 F.Supp. at 976 & n. 11.

2. Does the Control Held by the Governor Rise to the Level Necessary to be a "Municipality" Under Section 101(40)?

*23 The analysis then shifts to whether LVMC is an instrumentality of the State of Nevada. Is it, as *Webster's* stated, "something that serves as an intermediary or agent through which one or more functions of a controlling force are carried out: a part, organ, or subsidiary branch especially of a governing body"? To answer this question, LVMC's counsel urged the court to adopt the distinction between public function and public purpose. Public function is the large-scale and comprehensive treatment of a matter of traditional public concern, such as provided by police departments and public schools. Public purpose, on the other hand, is more diffuse in the sense that a private party can engage in an activity that has a public purpose, such as offering private security or charter schools. Enterprises with a public purpose augment and assist a larger public function, the charge of which is within the State's overall control.^{FN27}

While education, for example, may be a traditional governmental function, *see Ellicott School Bldg. Authority*, private charter schools are likely not instrumentalities because of the weak level of State control. Public transportation is also a traditional governmental function, *see Westport Transit District*, 165, although the regulation of private taxi companies would rarely be an occasion for labeling a taxi company an instrumentality of the State.^{FN28}

Another way to frame this question is to ask whether LVMC operates in place of the State or whether its operations are simply subject to regulation to ensure that LVMC's decisions further the public good. In this sense, regulation can be extensive and intrusive and not rise to the level of control required by Section 101(40). Casinos in Nevada, for example, are subject to wide-ranging and comprehensive regulation, but no one seriously contends that this regulation constitutes control sufficient to classify them as instrumentalities of the State.

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The tougher issues arise when, as here, there is an acknowledged governmental function, but the control is primarily strategic and periodic, rather than operational and constant. The State's ability and exercise of control over LVMC, both potentially and actually, is somewhat attenuated. While the Governor has the power to approve LVMC's fares, approve its budget and appoint its directors, LVMC operates its day-to-day business in significant isolation from the State. It has more than minimal competition from other government agencies, such as the RTC. It must apply for permission to operate from other public agencies. Its creditors are not, and do not expect to be, creditors of the State. It was created with the express and repeated promise that no taxes would be used to fund its operation. This low level of State control over matters going to essential state sovereignty and essential state functions indicates that LVMC is not a municipality as contemplated by the Bankruptcy Code.

LVMC thus has few of the attributes that would lead to its classification as a municipality under Section 101(40). The concerns for State sovereignty that underlie Chapter 9 are absent here. LVMC exercises no traditional public powers: it cannot tax; it cannot condemn by eminent domain; and it has no sovereign immunity. *Westport Transit District*, 165 B.R. at 95-96; *Shenango*, 80 B.R. at 415-16.

*24 It is beyond doubt that Nevada's involvement in LVMC is significant, and some might say too intrusive for LVMC to be purely private. But those intrusions are relatively unique, and not designed to protect public finances or the public fisc. While the elements of control are many—the Governor appoints LVMC's governing body, and has the right to veto its fares and budget—these controls go to the service LVMC provides and not to protection of Nevada's finances.

In this light, the controls in place are best viewed more like traditional regulation and less like sovereign specification of function. While the State of Nevada can guide LVMC's general course, it can do so only from afar and on a periodic basis. The day-to-day operations are still within the purview of LVMC's officers and employees, without any direct control from a State official. While the State of Nevada gets the benefit of added transportation options for its citizens and visitors, it is insulated from any great losses—for example, LVMC liabilities are not borne by the State; injuries caused during its operations are LVMC's liabilities, not the State's.

But more importantly, although Nevada, through its Governor, guides LVMC's budget and to a certain extent its management, the State is insulated from any of LVMC's operating losses. While the Bonds are obligations, albeit limited and nonrecourse obligations, of the State, the liability on the Bonds proper is not an issue in this case, as LVMC is not a party to and has not guaranteed payment on the Bonds. Rather, the focus of this case is LVMC's liability under the Financing Agreement and its other contracts with private parties such as Bombardier. As a consequence, this bankruptcy case at most affects the source of the Bonds' repayment, not repayment on the Bonds themselves.^{FN29} Indeed, that is precisely why the original offering included Ambac's insurance—to augment the sources of repayment. Moreover, this case affects not only LVMC's obligations related to the Bonds, but also Bombardier and to all LVMC's employees and other creditors.

These attributes all derive from the fact that LVMC was set up so that taxpayers would never have to fund it or its operations. LVMC has no taxing powers, and no independent power to issue obligations which bear tax-free interest. It has no power of eminent domain. It has no sovereign immunity. It has to obtain licenses and franchises just as if it were a purely private party.

LVMC thus bears the consequences of its operations in a manner similar to a private entity. *See, e.g.*, H.R.REP. NO. 2246, 79th Cong., 2d Sess. 2-3 (1946); S.REP. NO. 1633, 79th Cong., 2d Sess. 2 (1946). Its only revenues are those which come from operation of the monorail, and although its fare structure is set by the Governor, that fact is no more problematic for the instrumentality analysis than having insurance companies rate structures set by a State Department of Insurance, or having interest rates set by usury statutes. Government often controls or regulates how private entities earn their income. And although LVMC's expenses are limited by the combined effect of the budgetary process and the Governor's approval, the primary restriction on LVMC's ability to incur expense is the Indenture and the Trustee's oversight.

*25 The Governor's control, then, while extensive, is not the type of control that historically has caused courts to label entities or enterprises instrumentalities of the State. Indeed, given the thrust and mission of LVMC to be independent of the State and its sources of tax revenues, it is best seen as an entity engaged in a public purpose, not an instrumentality carrying out a public function.

3. Does Nevada Law Treat LVMC as One of Its In-

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strumentalities?

Finally, LVMC points to Ninth Circuit law that purportedly requires this federal court to give controlling effect to the labels used by State government. See *Security Bldg. & Loan Ass'n v. Spurlock*, 65 F.2d 768 (9th Cir.1933). *Spurlock* dealt with whether a building and loan association, denominated as such, was the type of "building and loan association" federal bankruptcy law excluded from being eligible to file a federal bankruptcy case. Although *Spurlock* held that the entity at issue was not eligible, it set no per se rules that federal courts must adopt State designations in such matters. As the court noted, "[n]o one would dispute, and it is not disputed here, that the definition of a building and loan association contained in the Arizona statute is in accord with the general conception of such organization throughout the United States." *Id.* at 772 (emphasis supplied). In other words, no one seriously contested, as is contested here, that the meaning of "building and loan association" was isomorphic in both State and federal laws.^{FN30}

There is, however, a nub of relevancy in this argument that requires some discussion. Historically, Congress has been very deferential to the ability of States to veto the participation by their municipalities in Chapter 9 arrangements; the 1994 amendments to the Bankruptcy Code underscore this point.^{FN31} It is thus relevant to examine Nevada's plan for distressed municipalities and examine whether that system applies here.

Nevada has systems for financially distressed public authorities, and thus denies its departments and agencies access to Chapter 9 in the case of financial need. The qualifications for this treatment, however, would exclude LVMC, making it look as though the State has little interest in whether it files for Chapter 11 or not. Specifically, Nevada law states that its financial distress provisions "apply to all local governments." Under Nevada law,

"Local government" means every political subdivision or other entity which has the right to levy or receive money from ad valorem or other taxes or any mandatory assessments, and includes, without limitation, counties, cities, towns, boards, school districts and other districts....

NEV.REV.STAT. § 354.474.1(a). Again, consistent with the origins of municipal bankruptcy, the key is the power to tax, a power that has been denied to LVMC. It is not the type of enterprise or public entity that Nevada has

provided for in the case of public distress.

*26 Analyzing the statutes regarding monorails and their operations further underscores these conclusions. Nevada's statutes specifically dealing with monorails contemplate that the monorail owner and operator would be a "person" under Nevada law. See NEV.REV.STAT. §§ 705.660, 705.665. Under Nevada law, a person means a natural person, corporation, or some other form of business organization other than a political subdivision or governmental agency. See NEV.REV.STAT. § 0.039. This exclusion indicates Nevada's intent that "persons" such as LVMC are not governmental entities.

Further, Section 705.690 provides in part that counties and cities may exercise their respective powers to "facilitate" the installation and operation of a monorail, and "contribute to" or "assist in the financing of" a monorail. Notably, the statute does not refer to cities and counties directly owning and operating a monorail nor does it refer to the taking on of any direct financial responsibility for them. The eligibility is open to all "persons."

In addition, one gets a hint that Nevada does not consider LVMC a municipality by looking at how it treats entities that are acknowledged municipalities. As with other States, Nevada has a complex and detailed scheme of laws dealing with public improvement projects and public works projects, and the counties and cities of the State of Nevada have broad authority to construct, own, operate, and manage various types of public improvements and various types of public works. See, e.g., NEV.REV.STAT. §§ 244.151, 244A.019, 271.265, 338.010. It is telling that none of these types of city or county powers were employed with respect to LVMC. Indeed, lest there be any doubt, § 705.690 specifically states that a monorail is not a public work and is not a public utility.^{FN32}

LVMC was formed under Chapter 82 of the Nevada Revised Statutes as a nonprofit public benefit corporation. In most particulars, Nevada nonprofit corporations have the same powers and duties as other corporations. One of these, while not controlling here, is that Nevada sought to make Chapter 11 bankruptcy available to all corporations formed under Chapter 82. See NEV.REV.STAT. § 82.466. There is no exception for monorail companies such as LVMC.

As a consequence, to the extent that federal interpretation of Section 101(40) of the Bankruptcy Code looks to State

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classification and categorization, Nevada statutory law would likely not imbue LVMC with sufficient municipal qualities to make LVMC a municipality.

III. CONCLUSION

Chapter 9 is a bankruptcy remedy restricted to municipalities. As used in the Bankruptcy Code, this term includes instrumentalities of the State. Ambac contends that LVMC is such an instrumentality, contending that the level of control held and exercised by the State is sufficient for that categorization under recent bankruptcy case-law and tax law.

Instrumentalities under Chapter 9, however, are unique, and can be understood only by an examination of the history of Chapter 9 eligibility. That examination reveals a concern not with regulation of matters of public interest, but a concern with the separateness and sovereignty of States, as exemplified through laws affecting traditional public functions and the public fisc.

*27 LVMC does not exhibit any of these characteristics to the extent required under the Bankruptcy Code or the caselaw interpreting it. Ambac's motion is denied.^{FN33}

Appendix 1-Definition of "Municipality" after 1937 Act

Selected Provisions of Act of August 16, 1937, Pub.L. No. 302, 50 Stat. 653 (1937)

SEC. 81. This Act and proceedings thereunder are found and declared to be within the subject of bankruptcies and, in addition to the jurisdiction otherwise exercised, courts of bankruptcy shall exercise original jurisdiction as provided in this chapter for the composition of indebtedness of, or authorized by, any of the taxing agencies or instrumentalities hereinafter named, payable (a) out of assessments or taxes, or both, levied against and constituting liens upon property in any of said taxing agencies or instrumentalities, or (b) out of property acquired by foreclosure of any such assessments or taxes or both, or (c) out of income derived by such taxing agencies or instrumentalities from the sale of water or power or both, or (d) from any combination thereof; (1) Drainage, drainage and levee, levee, levee and drainage, reclamation, water, irrigation, or other similar districts, commonly designated as agricultural improvement districts or local improvement districts, organized or created for the purpose of con-

structing, improving, maintaining, and operating certain improvements or projects devoted chiefly to the improvement of lands therein for agricultural purposes; or (2) local improvement districts such as sewer, paving, sanitary, or other similar districts, organized or created for the purposes designated by their respective names; or (3) local improvement districts such as road, highway, or other similar districts, organized or created for the purpose of grading, paving, or otherwise improving public streets, roads, or highways; or (4) public-school districts or public-school authorities organized or created for the purpose of constructing, maintaining and operating public schools or public-school facilities; or (5) local improvement districts such as port, navigation, or other similar districts, organized or created for the purpose of constructing, improving, maintaining, and operating ports and port facilities; or (6) any city, town, village, borough, township, or other municipality; *Provided, however,* That if any provision of this chapter, or the application thereof to any such taxing agency or district or class thereof or to any circumstance, is held invalid, the remainder of the chapter, or the application of such provision to any other or different taxing agency or district or class thereof or to any other or different circumstances, shall not be affected by such holding.

SEC. 82. The following terms as used in this chapter, unless a different meaning is plainly required by the context, shall be construed as follows:

That the term 'petitioner' shall include any taxing agency or instrumentality referred to in section 81 of this chapter.

Appendix 2-Definition of "Municipality" after 1946 Act

Selected Provisions of the Act of July 1, 1946, Pub.L. 481, 60 Stat. 409

*28 SEC. 81. This Act and proceedings thereunder are found and declared to be within the subject of bankruptcies and, in addition to the jurisdiction otherwise exercised, courts of bankruptcy shall exercise original jurisdiction as provided in this chapter for the composition of indebtedness of, or authorized by, any of the agencies or instrumentalities hereinafter named, payable (a) out of assessments or taxes, or both, levied against and constituting liens upon property in any of said agencies or instrumentalities, or (b) out of property acquired by foreclosure of any such assessments or taxes or both, or (c) out of income derived by such agencies or instrumentalities

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from any income-producing property, whether or not secured by a lien upon such property: (1) Drainage, drainage and levee, reclamation, water, irrigation, or other similar districts, commonly designated as agricultural improvement districts or local improvement districts, organized or created for the purpose of constructing, improving, maintaining, and operating certain improvements or projects devoted chiefly to the improvement of lands therein for agricultural purposes; or (2) local improvement districts, such as sewer, paving, sanitary, or other similar districts, organized or created for the purposes designated by their respective names; or (3) local improvement districts, such as road, highway, or other similar districts, organized or created for the purpose of grading, paving, or otherwise improving public streets, roads, or highways; or (4) public-school districts or public-school authorities organized or created for the purpose of constructing, maintaining, and operating public schools or public-school facilities; or (5) local improvement districts, such as port, navigation, or other similar districts, organized or created for the purpose of constructing, improving, maintaining, and operating ports and port facilities; or (6) incorporated authorities, commissions, or similar public agencies organized for the purpose of constructing, maintaining, and operating revenue-producing enterprises; or (7) any county or parish or any city, town, village borough, township, or other municipality; *Provided, however*, That if any provision of this chapter, or the application thereof to any such agency or district or class thereof or to any circumstance, is held invalid, the remainder of the chapter, or the application of such provision to any other or different circumstances, shall not be affected by such holding.

SEC. 82. The following terms as used in this chapter, unless a different meaning is plainly required by the context, shall be construed as follows:

The term 'petitioner' shall include any agency or instrumentality referred to in section 81 of this chapter.

FN1. LVMC is a private, nonprofit corporation, formed under Nevada's nonprofit corporation law. Its income is exempt from taxation under 26 U.S.C. § 503(c)(4). LVMC's articles of incorporation state that LVMC is not organized for profit, and that no part of its net earnings can "inure to the benefit" of any individual or entity other than the State of Nevada or one of its agencies.

FN2. The Bonds were issued in series. The first

series of Bonds have a principal amount of approximately \$450 million, and have the benefit of insurance (of which more later). Two junior series of the Bonds make up the remainder of the original \$650 million financing. These series are not secured and in some respects are contractually subordinate to the first series. US Bank has been appointed as an Indenture Trustee to represent the interests of the holders of the two junior series of Bonds.

FN3. The level of control is fairly expansive. LVMC's by-laws allow the Governor of Nevada to (i) inspect and audit LVMC's books and records on an annual basis; (ii) disapprove of any by-law amendment; (iii) disapprove of LVMC's rate schedule; and (iv) reject LVMC's annual budget, including any proposed capital expenditures. More importantly, the Governor can reject proposed board members, refuse to reappoint existing board members, and remove such directors for cause.

FN4. Its primary expense is its operating agreement with Bombardier Transit Corporation ("Bombardier"), which operates and services the trains. As LVMC is regulated as a private corporation under applicable Nevada law, some of its other expenses include obtaining necessary licenses and permits from governmental agencies to operate its business.

FN5. Ambac estimates that its exposure over the life of the bond issue is about \$1.16 billion.

FN6. The definition of "municipality" is somewhat redundant in that it includes an "instrumentality of the State," which is a phrase the Code already uses in Section 101(27)'s definition of "governmental unit."

FN7. This court has previously written on the standard tools of statutory interpretation. *See, e.g., In re Slusher*, 359 B.R. 290, 295-96 (Bankr.D.Nev.2007); *In re Trejos*, 352 B.R. 249, 254-259 (Bankr.D.Nev.2006), *aff'd*, 374 B.R. 210 (B.A.P.2007); *In re Kane*, 336 B.R. 477, 486-88 (Bankr.D.Nev.2006).

FN8. WEBSTER'S THIRD NEW INTERNATIONAL DICTIONARY, UNABRIDGED

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(Merriam-Webster 2002), available at <http://unabridged.merriam-webster.com> (last visited Mar. 31, 2010). The *Oxford English Dictionary* is similarly vague: “The quality or condition of being instrumental; the fact or function of serving or being used for the accomplishment of some purpose or end; agency.” OXFORD ENGLISH DICTIONARY (2d ed.1989), available at <http://dictionary.oed.com> (last visited Mar. 31, 2010)

FN9. In the Ninth Circuit, “[t]here are no sharp criteria for determining whether an entity is a federal agency within the meaning of the [Federal Tort Claims] Act, but the critical factor is the existence of federal government control over the ‘detailed physical performance’ and ‘day to day operation’ of that entity.” *Kuntz v. Lamar Corp.*, 385 F.3d 1177, 1184 (9th Cir.2004) (quoting *Lewis v. United States*, 680 F.2d 1239, 1240 (9th Cir.1982)).

FN10. States are subject to the Contracts Clause, U.S. CONST., Art. I, § 10, which limits their ability to modify contracts among their citizens. *Brown v. Smart*, 145 U.S. 454, 12 S.Ct. 958, 36 L.Ed. 773 (1892) (Contracts Clause prohibits state insolvency law from affecting the contractual rights of the citizens of other states without their consent). The federal government, however, is not subject to that clause, *Pension Benefit Guaranty Corp. v. R.A. Gray & Co.*, 467 U.S. 717, 732, n. 9, 104 S.Ct. 2709, 81 L.Ed.2d 601 (1984), and thus debtors in a federal bankruptcy action can and often do modify contracts with other parties. See, e.g., 11 U.S.C. § 365.

FN11. This act was later upheld by the Supreme Court. *United States v. Bekins*, 304 U.S. 27, 58 S.Ct. 811, 82 L.Ed. 1137 (1938). The decision was decided by a 6-2 vote. The dissenting justices were Mr. Justice McReynolds, the author of *Ashton*, and Mr. Justice Butler. Mr. Justice Cardozo, author of the dissent in *Ashton*, did not participate in *Bekins*.

FN12. Viewed through the lens of this case, these amendments would have made the Department an eligible Chapter IX debtor.

FN13. The Conference Report also referred to

statements of Rep. Edwards, the floor manager of the bill, made during the House debate with respect to the status of industrial revenue bond financing. H.R.REP. NO. 94-938 at 15. During that debate, when pressed about the status of such assets, Rep. Edwards stated:

We intend that claims that arise by virtue of these bonds not be among the claims allowable ... and that amounts owed by private companies to the holders of industrial revenue bonds are not among the assets of the municipality that are to be dealt with by the plan. *These transactions should really be handled outside the Chapter IX case.*

121 CONG. REC. 39,412 (1975) (emphasis supplied).

FN14. As noted at the time, Congress believed that the statements of the floor managers imbued Rep. Edwards and Sen. DeConcini's remarks with “the effect of being a conference report.” 124 CONG. REC. 32,376 (1978) (statement of Rep. Rousselot). As the Supreme Court subsequently noted: “Because of the absence of a conference and the key roles played by Representative Edwards and his counterpart floor manager Senator DeConcini, we have treated their floor statements on the Bankruptcy Reform Act of 1978 as persuasive evidence of congressional intent.” *Begier v. IRS*, 496 U.S. 53, 64 n. 5, 110 S.Ct. 2258, 110 L.Ed.2d 46 (1990).

FN15. *Kerr* was a civil rights case in which the issue of the status of the entity was relevant for the state action doctrine under the Fourteenth Amendment.

FN16. The district court in *Shenango* did not quibble with the bankruptcy court's analysis of whether the entity was a municipality. It reversed, however, based upon its conclusion that Pennsylvania law did not authorize the municipality to file a Chapter 9 petition.

FN17. *Pleasant View* relied on TENN.CODE § 7-82-301, which provided in relevant part:

From and after the date of the making and fil-

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ing of an order of incorporation, the district so incorporated shall be a "municipality" or public corporation in perpetuity under its corporate name, and the district shall in that name be a body politic and corporate with power of perpetual succession, but without any power to levy or collect taxes. Charges for services authorized in this chapter shall not be construed as taxes. The powers of each district shall be vested in and exercised by a majority of the members of the board of commissioners of the district.

FN18. In this respect, the entity seems to be similar to the debtor in *In re Cottonwood Water and Sanitation Dist., Douglas County, Colo.*, 138 B.R. 973 (Bankr.D.Colo.1992), in which no issue of the status of the debtor as a municipality was raised.

FN19. See, e.g., 26 U.S.C. § 4217 ("For purposes of this chapter, the lease of an article (including any renewal or any extension of a lease or any subsequent lease of such article) by the manufacturer, producer, or importer shall be considered a sale of such article); 26 U.S.C. § 4002(c)(1) (for purposes of excise taxes on luxury vehicles, "the lease of a vehicle (including any renewal or any extension of a lease or any subsequent lease of such vehicle) by any person shall be considered a sale of such vehicle at retail.").

FN20. The Offering Statement contained, on page 75, the following sentence: "Although the Company has no present intention to institute bankruptcy proceedings or protection under any other debtor relief laws, it may not be prevented from instituting such proceedings or seeking such relief or protection."

FN21. "Instrumentality" is used in many other contexts in federal law. As noted earlier, it forms part of the definitions used in the Foreign Sovereign Immunities Act. See *First Nat'l City Bank*, 462 U.S. at 624; 28 U.S.C. § 1603(a). It forms part of the definition of government plan under ERISA. See *Berini v. Federal Reserve Bank of St. Louis, Eighth District*, 420 F.Supp.2d 1021 (E.D.Mo.2005); 29 U.S.C. § 1002(32). It plays a role in sovereign immunity under the Federal Tort Claims Act. *Kuntz v. Lamar Corp.*, 385

F.3d 1177, 1184 (9th Cir.2004). And, relevant here, it also forms part of the analysis as to whether entities or enterprises must pay federal employment taxes on wages; instrumentalities of States are exempt. See, e.g., 26 U.S.C. § 3121(b)(7) (exemption from social security for employees of State instrumentalities); *id.* § 3306(c)(7) (exemption from federal unemployment tax for employees of State instrumentalities).

FN22. A revenue ruling is "an official interpretation by the Service that has been published in the Internal Revenue Bulletin ... for the information and guidance of taxpayers, Internal Revenue Service officials, and others concerned." *Treas. Reg. § 601.601(d)(2)(i)(a)*. Revenue rulings "do not have the force and effect of Treasury Department Regulations ..., but are published to provide precedents to be used in the disposition of other cases, and may be cited and relied upon for that purpose." *Id.* § 601.601(d)(2)(v)(d).

The Ninth Circuit states that the deference required for a Revenue Ruling "depends on the 'thoroughness evident in [the agency's] consideration, the validity of its reasoning, its consistency with earlier and later pronouncements, and all those factors which give it the power to persuade ...'" *Omhundro v. United States*, 300 F.3d 1065, 1068 (9th Cir.2002) (quoting *United States v. Mead Corp.*, 533 U.S. 218, 228, 121 S.Ct. 2164, 150 L.Ed.2d 292 (2001) (citing *Skidmore v. Swift & Co.*, 323 U.S. 134, 140, 65 S.Ct. 161, 89 L.Ed. 124 (1944))).

By contrast, the Tax Court characterizes a revenue ruling as the IRS's litigation position, which carries no more weight than any well-reasoned argument. See, e.g., *McLaulin v. Comm'r*, 115 T.C. 255, 263, 2000 WL 1349154 (2000); *Norfolk S. Corp. v. Comm'r*, 104 T.C. 13, 45-46, 1995 WL 9185 (1995).

FN23. The IRS also indicated that a private non-stock corporation formed by private individuals was not an instrumentality, even though State officials were authorized to assist it in carrying out its functions. The owners controlled the entity, although the State paid them a monthly fee to at-

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tend board meetings. Finding that the entity was formed for private purposes, and that the State's involvement was no more than general regulation, the IRS stated that the entity was not an instrumentality. Rev. Rul. 69-453, 1969-2 C.B. 192.

FN24. Professor Aprill states that this test:

differ[s] somewhat from th[at] established by Revenue Ruling 57-128 for the payroll tax provisions.... In addition to control over the organization's everyday operations, Rev. Rul. 89-49 lists the following factors: "(1) whether there is specific legislation creating the organization; (2) the source of funds for the organization; (3) the manner in which the organization's trustees or operating board are selected; and (4) whether the applicable governmental unit considers the employees of the organization to be employees of the applicable governmental unit."

Ellen P. Aprill, *The Integral, the Essential, and the Instrumental: Federal Income Tax Treatment of Governmental Affiliates*, 23 J. CORP. L. 803, 822 n. 162 (1998).

FN25. To the extent that Ambac has commended Professor Aprill's excellent analysis, it appears that LVMC would not meet the instrumentality test suggested by her article. Her article suggestions looking to 26 U.S.C. § 502(c)(27) and its four-part test to assess whether an enterprise or organization is an instrumentality for tax purposes. Aprill, 23 J. CORP. L., at 835 ("The four requirements of section 501(c)(27) regarding creation, control, initial financial commitment, and destination of assets upon dissolution embody the most important requirements underlying exemption for integral parts, section 115 entities, and instrumentalities.... These four conditions could-and should-apply to all governmental affiliates seeking exemption from federal income tax."). LVMC, however, would appear to fail the initial financial commitment condition-since its funding came from a public bond offering, and its current operating revenues come from passenger fares-and these fares exceed its operating expenses (although are not enough to meet its scheduled debt service). As the conditions of 26

U.S.C. § 502(c)(27) are conjunctive, LVMC would appear to fail the proposed test.

FN26. LVMC has an exemption under 26 U.S.C. § 501(c)(4), which is given to "[c]ivic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare...."

FN27. In one sense, it is a public function to provide financing for public works, but a public purpose to work with the State in the creation and operation of these public works. That is the distinction here; the Department is most certainly an agency of the State of Nevada, charged, among other things, with the public function of providing financing for public purposes, such as transportation. LVMC, in contrast, is part of the provision of that public function, but only a part; the traditional entity charged with fulfilling the transport public function is the RTC. See *Westport Transit Dist.*, 165 B.R. at 95-96 (finding that entity was municipality rested in part on the entity's power of eminent domain, the power to directly issue bonds, and the power to set its own fares).

FN28. Similarly, States regulate insurance companies' rates, as well as the content of their policies, yet no one argues that this intrusive level of control transmutes insurance companies into State instrumentalities.

FN29. Some observers might see this argument as sophistry. If the Bonds are nonrecourse and payable only from the amounts LVMC is liable for under the Financing Agreement, then saying that liability on the Bonds is not affected by LVMC's ability to modify its debt under the Financing Agreement is, so the argument goes, a distinction without a difference. Indeed, as shown above, tax law explicitly ignores this formality.

But holders of the Bonds have at least two sources of repayment: Ambac's insurance would not be affected by any adjustments to LVMC's obligations under the Financing Agreement. In the grand scheme of things, assuming Ambac's solvency, adjustments to LVMC's obligations under the Financing

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Agreement simply shift the payment obligations to Ambac, a shift that Ambac agreed to and was paid to undertake.

FN30. Even if *Spurlock* could be read as LVMC urges, the Supremacy Clause would make short work of the argument. Courts incorporate definitions from State law into federal law only advisedly, and then only when necessary to effect congressional intent. Cf. *Kamen v. Kemper Fin. Servs., Inc.*, 500 U.S. 90, 98, 111 S.Ct. 1711, 114 L.Ed.2d 152 (1991) (discussing that incorporated State terms must not be construed to override federal policy concerns); *Americredit Fin. Servs., Inc. v. Penrod (In re Penrod)*, 392 B.R. 835, 843 (B.A.P. 9th Cir.2008) (discussing role of federal law in interpreting undefined phrases in federal law that are defined in similar contexts under State law).

FN31. This veto ability assuages some of the constitutional concerns inherent in allowing a federal court to dictate how a State should manage its internal affairs when there is no countervailing federal policy involved.

FN32. The parties also acknowledged this implicitly in the Indenture. The remedies section of that agreement, Section 7.02(d), specifically refers to the Trustee's right to appoint a receiver, a remedy not available for any State instrumentality.

FN33. This opinion shall also serve as the court's findings of facts and conclusions of law under FED. R. BANKR.P. 7052, applicable to this contested matter by FED. R. BANKR.P. 9014(c).

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