



TAMPA BAY BANKRUPTCY CENTER, P.A.

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The Other Side of State Bankruptcies

Former House Speaker Newt Gingrich is all for having legislation that allows states to file for bankruptcy protection. Gingrich says that doing so would free state governments from their crippling debts and allow them to rebuild their finances. It would also cause state governments not to always approach the federal government for bailout funds. Although it seems a logical and simple solution to the financial problems of cash-strapped state governments, is there more than meets the eye?

Many do not realize that there are other options state governments have to reduce their deficits. For example, the state of Illinois just enacted a temporary state income tax increase to help close its budget gap. Likewise, California has initiated wage cuts and tax extensions in its struggle to overcome its \$25 billion deficit.

Gingrich contends that the ability to file for bankruptcy would give state governments a greater bargaining power over labor unions who can be unreasonable with their demands. But whether or not a state is in bankruptcy, if it cannot pay its workers, everybody loses. Hence, labor unions would naturally have an incentive to compromise with state governments. In fact, some labor union bosses have already agreed to make concessions on benefits for new workers.

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Another result of a bankruptcy filing for a state government would be an exit from capital markets. This would cut off a vital source of income for state governments and leave them having to search for other funding sources to finance infrastructure development and provide much needed revenue. For instance, California would need \$10 billion annually to meet its cash flow needs.

In addition, legal bankruptcy overseen by the federal government goes against the constitution as each state is considered a sovereign entity. Such bankruptcy would also cost a huge amount of money for the states. Even when a city files for bankruptcy, it is an expensive affair, as can be seen in the case of Vallejo in California that filed for bankruptcy in 2008. It has spent about \$9.5 million in legal fees thus far without an end in sight as the court case is still ongoing.

Lastly, if a state government is in bankruptcy, it would not be able to autonomously increase taxes. Hence, it would naturally mean that the state would have to rely on federal funding to see itself through the bankruptcy period, something declaring bankruptcy was meant to avoid in the first place.

Unlike the case with state governments, individual citizens have the right to seek bankruptcy protection and many have done so. If you wish to file for bankruptcy, call us at (813) 200-4133 for a free consultation.