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The Judiciary and Fiscal Crises: An Institutional Critique

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The Judiciary and Fiscal Crises: An Institutionalist Critique

Ronald J. Gilson
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January 2014

THE JUDICIARY AND FISCAL CRISES: AN INSTITUTIONALIST CRITIQUE

Peter Conti-Brown ·

Ronald J. Gilson **

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Abstract: Scholars have long debated the role for courts with respect to governmental action that responds to crisis. Most of the crises analyzed, however, are *exogenous* to the political process; the courts' role in response to politically *endogenous* crises has received less attention. We evaluate the role of the judiciary in a subset of those endogenous crises: the judicial treatment of governmental efforts to resolve the crisis facing underfunded public pensions. Assessing institutional competence schematically with reference to an institution's democratic accountability and fact-finding ability, we argue that, where institutions function properly, judicial intervention in politically endogenous economic crises should be close to nonexistent. But when they must occur—and, consistent with doctrines of justiciability, some adjudication of governmental action in the fiscal context will be inevitable—we argue that such intervention should respect the judiciary's comparative institutional incompetence by treading lightly, constitutionally speaking: where the relevant law allows discretion, and where a non-constitutional determination is possible, courts addressing the state's fiscal policy-making apparatus should avoid constitutional pronouncements entirely.

After developing a preliminary framework for assessing this decision rule, we apply it to a hard case (where the statute and contract is silent as to whether executory pension contracts are

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subject to constitutional protection against modification) and an easy case (where there is a reservation of rights for that very modification). Unfortunately, courts have erred in both the hard and easy cases; our framework explains why the law is not only consistent with our decision rule, but why comparative institutional competence compels the result. In both the easy and the hard cases, the point is not to promote or demote the interests of a single class or faction active within the fiscal policy-making process—whether bondholders, public unions, taxpayers, or the government—but to locate that policy-making process within the most democratically responsive and empirically competent institutions. With this framework, we evaluate the recent effort of the San Jose Superior Court to address these issues. We conclude that the court got the easy case exactly wrong.

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INTRODUCTION

The recent financial crisis has led to an important debate among scholars and policy-makers regarding the authority and efficacy of various institutions—whether the President, courts, Congress, and others—in responding to the exigencies of such crises.¹ There is nothing new, of course, in comparative analysis of institutional competence.² What is new, or at least resurgent, is institutional comparison in the context of crises.³ When the stakes are high and time for decision-making is short, the question of which institution should be

¹ ERIC A. POSNER & ADRIAN VERMEULE, *THE EXECUTIVE UNBOUND: AFTER THE MADISONIAN REPUBLIC* 54 (2010) [hereinafter Posner & Vermeule]

² NEIL K. KOMESAR, *IMPERFECT ALTERNATIVES: CHOOSING INSTITUTIONS IN LAW, ECONOMICS, AND PUBLIC POLICY* (1994).

³ David A. Skeel Jr., *Institutional Choice in an Economic Crisis*, 2013 WISC. L. REV. 629 (2013).

on the frontline demands attention.

To date, the effort to understand and recommend specific candidates for first-response has focused largely on the governmental response to *exogenous* crises.⁴ These crises include terrorist attacks, financial crises, natural disasters, or any other event arising outside of the system that becomes acute suddenly and requires swift governmental reaction. Political and legal machinery will churn in the face of such crises. It is the policy processes and products that are deployed in the face of those exogenous crises that have animated almost all of the recent attention. The “judicial question,” in this context, is what role, if any, should courts have in making policy or checking the conduct of other governmental actors in crisis.

This debate about institutional response to exogenous crises is important and informative. But not all crises that result in the invocation of judicial authority come in response to exogenous crises. Some crises, and arguably most fiscal crises, are *endogenous*. In exogenous crises, the government’s role is to respond to a crisis that, definitionally, comes from the outside. In endogenous crises, the government must respond to the crisis that it created. In exogenous crises, society expects prompt action and then—only after resolution—inquiries into causes, prevention, and accountability. In endogenous crises, there can be no such separation. The crisis is the political system; the political system is responsible for the reaction.

Fiscal crises involving the overcommitment and underfunding of public pensions are a powerful example of such politically-endogenous crises.⁵ To take a step back, political institutions—the legislature and executive where such a separation exists, a unified body like a city council where it does not—must assess the proper level of taxation and spending, responsive to and constrained by the demands of the electorate. When political actors cannot do so sustainably, a profound mismatch between revenues and expenditures results. The mismatch, if not remedied, becomes the self-induced fiscal crisis that is endogenous to the political process—political institutions set the size of future pension payments, determine the necessary funding and impose the taxes that fund the pensions.

⁴ Posner & Vermeule, *supra* note 1, at 31.

⁵ To be sure, exogenous factors such as economic recession or financial crises can contribute to the immediacy of the endogenous crisis. But even in those situations, a political resolution—through decreased services and increased revenues—can be sought. The inability to resolve the problem, in most cases, reflects a political breakdown, not an economic one.

A shift in focus from exogenous to endogenous crises thus frames our inquiry: what are the appropriate roles of different institutions, in particular the courts, when the crisis is internal to the political process itself? In this essay, we address the current public pension crisis as a lens through which to analyze the role of courts in endogenous crises generally. To address the question of institutional competence in the context of endogenous crises, we define institutional competence as the intersection of the extent of an institution's democratic legitimacy and its fact-finding capacity. Generally, we argue, the institution with the greatest competence is the one for whom the combination of these two criteria is higher than alternative institutions. We will see that the most institutionally competent actors to address fiscal crises will be the political institutions. Fiscal policy-making is at the heart of their political roles; the judiciary is institutionally ill-suited to make the kinds of political tradeoffs that inhere to the fiscal policy-making process.

Given the lack of competence, one might hope for complete judicial non-participation in the resolution of fiscal crises. But the fiscal policy process is fraught with controversy. The process yields political winners and losers, and the losers, as in any legal context, are likely to invoke the jurisdiction of the courts to press the policy case they have lost in the political arena. Where that jurisdiction is invoked consistent with doctrines of justiciability, the courts will become the next frontline for conflicts over fiscal policy.

Thus adjudication over fiscal conflicts is inevitable. And ours is not an argument in favor of a more limited doctrine of standing or a more expansive political question doctrine, either of which would limit judicial participation in fiscal policy. Instead, we argue for a decision rule that will guide courts with valid jurisdiction in response to fiscal crises. The rule is to tread lightly, constitutionally speaking: absent clear violation of uncontroversial legal rights, courts should stay out of the business of fiscal policy-making. Judicial interventions in fiscal policy should be rendered in a way that allows political revision in the usual course, without constitutional amendment. Such a constitutional soft touch forces the issue back to the political branches. In this formulation, the judicial role is to do no more than allocate the burden of political resolution back to the politically accountable institutions to continue the negotiation of fiscal policy-making.

To demonstrate our argument, we present two cases, one hard, the other easy. The hard case is one of the central legal issues that directly bears on fiscal crisis-driven pension litigation: the so-called

“California Rule” applicable in California and twelve other states.⁶ The term refers to a state court doctrine that subjects prospective pension assurances to the Contracts Clause of the U.S. Constitution and its state-constitution equivalents, such that states are prevented from reducing prospective pension accruals to current employees; that is, not the amount of an employee’s future benefits that have already vested, but the rate at which future benefits for work as yet unperformed are earned.

We look closely at the legal and economic context of the California Rule and acknowledge that interpreting the terms of the public employees’ contract—necessary to determine whether that contract is protected by the Contracts Clause—is hard but also recognizing there are circumstances where both parties might indeed want to be bound, constitutionally, by a contract with such peculiarly restrictive terms. But the California Rule does not follow from these interpretive difficulties: we argue that because the courts lack the institutional competence to make fiscal policy, they should not create or expand doctrines that ossify the fiscal policy-making process in the way that the California Rule does. Thus, our institutionalist framework directs that the court to avoid a constitutional determination that has the dual debilities of removing fiscal resolution from the political process and of tying the hands of future political actors in the process. We explain how this result is fully consistent with the courts’ broad discretion in the Contracts Clause context.

The easy case is perhaps more important, both because it is under active litigation, and because the only trial court to address it got the question exactly wrong. As we explore in more detail below, most statutory language creating the public employee contract is ambiguous as to whether it should be subject to the Contracts Clause. Some statutes, however, explicitly reserve the right to make prospective changes to unaccrued benefits. In the latter case, the California Rule not only doesn’t require constitutional protection for such contracts—the rule is, after all, one of statutory construction—but doesn’t apply at all: changes in future pension accruals do not abrogate the terms of the contract. The Santa Clara County court’s opinion illustrates not only the illogic behind a contrary decision, but also the consequences of such an opinion: the court’s seemingly Solomonic decision inserts the judiciary into the grit of fiscal policy-making—who gets what, when, and why—a work it is institutionally ill-suited to perform.

The essay proceeds as follows. Part I goes into more detail re-

⁶ The states include Washington, Colorado, Massachusetts and Pennsylvania. See Amy B. Monahan, *Statutes as Contracts? The “California Rule” and Its Impact on Public Pension Reform*, 97 IOWA L. REV. 1029, 1071 (2012) [hereinafter Monahan]

garding the intersection of endogenous crises and the institutions that respond to them. Unlike recent literature that focuses on the role of the executive and the relative irrelevance of legal restrictions—including judicial efforts to restrict executive action—in exogenous crises we argue that endogenous fiscal crises are quite distinct from exogenous financial or national security crises, but that courts nonetheless remain institutionally less competent than political institutions to address them. We set out the institutional competence framework, and explain why even less competent institutions still have a role to play. We then describe the decision rule that should guide that intervention: the court’s proper goal is to create as broad a space possible for fiscal policy-making, so as to force the political institutions to continue to address such policy directly. The opposite result, the constitutionalization of fiscal policy-making that the California Rule dictates, significantly restricts the fiscal policy-making space and displaces the institutions best situated to create such policy.

Part II then applies the institutional competence framework to the hard case, that of statutory ambiguity as to the applicability of the Contracts Clause to purely executory contracts. After briefly explaining the California Rule, we address why, as a matter of law and economics, the constitutional treatment of unvested pension promises is difficult for a number of reasons, including, for example, California’s long adherence to the California Rule (which creates and alters parties’ expectations in the course of bargaining and strengthens its value as precedent). Although we view the legal issue as harder than do other critics, we think even reasonable disagreement indicates the need to remove the courts from the fiscal-policy process by limiting them to a decision that can be reversed through the normal political process. Institutionally, the better approach is for courts to force more competent political institutions to resolve the contractual status of unvested benefits through private negotiation, electoral politics, or strategic action, such as default on the government’s part or strikes by the public employees. This judicial deference to political-fiscal institutions thus allows the costs and benefits of fiscal policy-making to be fully born by politically accountable actors. Here again, San Jose provides an instructive example.

Part III then applies our framework to what should be an easy case: where the statutes specifically allow the government to make alterations to prospective contracts, the government has a free hand for prospective modification free of constitutional restriction. As easy as this case it is, it is also in some ways the more important. This very case is under appellate review in the California courts and, for reasons we discuss in Part III, the trial court both got the answer wrong and demonstrates the consequences of judicial intervention in

the fiscal policy-making process. The California Supreme Court’s eventual resolution of the easy case will reverberate throughout the country as states and cities continue to attempt a political resolution to a political problem: the allocation of revenues to services, compensation, and retirement benefits in a way that is fiscally sustainable.

I. INSTITUTIONAL COMPETENCE AND FISCAL CRISIS

A. *Context of Institutional Comparison*

The question of institutional competence cannot be answered in the abstract, but only in response to a specific problem, in our case, the need to respond to an endogenous fiscal crisis: which institution among available alternatives can best resolve the crisis? Neil Komesar presents a useful frame for analyzing an institution’s fit with a particular problem.⁷ Under the Komesarian analysis, the question of institutional fit is inherently a comparative one:

Issues at which an institution, in the abstract, may be good may not need that institution because one of the alternative institutions may be even better. In turn, tasks that strain the abilities of an institution may wisely be assigned to it anyway if the alternatives are even worse.⁸

As David Skeel has recently argued, scholars have invoked the Komesarian analysis for the everyday business of public policy, including dispute resolution. What is missing is an explanation of how this institutional comparison is changed, perhaps radically, by the existence of a crisis.⁹ Attributes such as speed of reaction and capacity for detailed fact-finding may figure differently in the analysis when circumstances are more extreme. However, even as crisis changes the relative importance of specific institutional attributes, it does not change the core of the comparative analysis: to locate the most effective institutional alternative for resolving a specific public policy dispute. That goal remains, even in a crisis, a relative, not an absolute,

⁷ See generally KOMESAR, *supra* note 2. For related analyses, see Howard S. Erlanger & Thomas W. Merrill, *Institutional Choice and Political Faith*, 22 LAW & SOC. INQUIRY 959, 963 (1997); Richard J. Price, Jr., *Public Utility Regulatory Takings: Should the Judiciary Attempt to Police the Political Institutions?*, 77 GEO. L.J. 2031, 2040 (1989)

⁸ KOMESAR, *supra* note 2.

⁹ Skeel, *supra* note 3.

inquiry.

To be sure, the presence of a crisis can shift the institutional comparison in favor of the institution best able to act decisively in the face of crisis, even in the face of legal prohibition or institutional deficiencies that would loom large absent the crisis. Posner and Vermeule take this position: descriptively and prescriptively, the executive—including the administrative agencies that the executive ostensibly oversees—will be best situated to respond to crises consistent with popular sentiment, even if not always consistent with law.¹⁰ Particularly when the legal system will be available to sort out after the fact the consequences of swift if debatably lawful institutional actions, the existence of the crisis may privilege speed over certainty of authority.

Posner and Vermeule's institutional defense of the executive is not without critics.¹¹ But we need not engage that debate here. The comparative institutional evaluation of interest to those scholars takes place in the face of *exogenous* crises: that is, crises that are largely not creations of the political institutions themselves, but require their quick response. We are concerned with *endogenous* crises, where the crisis is itself a result of a political process.

Before proceeding, it is important to acknowledge that the distraction between endogenous and exogenous crises may blur at the margin. The 2008 financial crisis illustrates the point well. Critics from the left and right have highlighted several actions, ranging from the repeal of Glass-Steagall,¹² to changes in SEC leverage requirements,¹³ to the Congressional support for government-sponsored enterprises Fannie Mae and Freddie Mac¹⁴ or the Fed's monetary poli-

¹⁰ The role of the Treasury and Federal Reserve, in the context of the recent financial crisis, in influencing the Bank of America to close its acquisition of Merrill Lynch without the delay that would be associated with recirculating the proxy statement to approve the transaction in light of arguably material new information poses this issue nicely. Merrill Lynch would have failed absent the transaction at a time when the government believed that such a failure would threaten the financial system.

¹¹ See Saikrishna B. Prakash & Michael D. Ramsey, *The Goldilocks Executive*, 90 TEXAS L. REV. 973 (2012).

¹² Cyrus Sinati, *10 Years Later. Looking at the Repeal of Glass-Steagall*, N.Y. TIMES DEALBOOK (Nov. 12, 2009), http://dealbook.nytimes.com/2009/11/12/10-years-later-looking-at-repeal-of-glass-steagall/?_r=0

¹³ Alan S. Blinder, *Six Errors on the Path to the Financial Crisis*, N.Y. TIMES (Jan. 24, 2009), <http://www.nytimes.com/2009/01/25/business/economy/25view.html>

¹⁴ Nick Timiraos, *Five Years Later, Fannie Mae and Freddie Mac Remain Unfinished Business*, WALL ST. J. (Sept. 6, 2013), <http://online.wsj.com/article/SB10001424127887323423804579022672911329450.html>

cies in the early 2000s,¹⁵ which, with the benefit of hindsight, might have averted or moderated the 2008-2009 financial crisis. Indeed, almost tautologically, hindsight renders government action or inaction inherently a cause of financial crises—the government could have acted or could have acted differently. In invoking the endogenous/exogenous taxonomy, though, we distinguish between cases where the government may *contribute* to an exogenous financial crisis, and those, as with fiscal crises, where the government *is* the crisis. The endogeneity of fiscal crises remains the governing framework even when, as will almost always be the case, economic recession or financial crisis magnifies the fiscal panic. Because the fiscal policy-making apparatus remains in control of optimizing revenues and expenditures, the inability to bring the two into balance still reflects a breakdown of that central political process. A comparative institutional assessment in the face of politically endogenous crises is the focus of our inquiry.

B. *Public Pensions*

There is no question that the American states are facing a profound mismatch between commitments to public pensions and the funding devoted to support those commitments.¹⁶ The gap between the amount promised to present and future retirees and the funds on hand to honor those promises is staggering. By one estimate, that mismatch amounts to between \$3 and \$5 trillion, or between \$27,000 and \$45,000 per American household.¹⁷ The extent of this fiscal mismatch reflects much more than public pensions: it is a fundamental breakdown in the entire fiscal apparatus manifested by a combination of a preference for both low taxes and high services. As one commentator colorfully put it, some citizens expect to be “taxed like libertarians, but subsidized like socialists.”¹⁸ In California alone, one source estimates the current unfunded pension liability as ranging from \$10.53 billion, or \$885 per California household, using a 9.5% discount rate, to \$497.9 billion, or \$40,850 per household, using a

¹⁵ John B. Taylor, *How Government Created the Financial Crisis*, WALL ST. J. (Feb. 9, 2009), <http://online.wsj.com/article/SB123414310280561945.html>

¹⁶ See generally Olivia Mitchell, *Public Pension Pressures in the United States*, in WHEN STATES GO BROKE: THE ORIGINS, CONTEXT, AND SOLUTIONS FOR THE AMERICAN STATES IN FISCAL CRISIS (Peter Conti-Brown & David Skeel eds., 2012)

¹⁷ Monahan *supra* note 6 at 1031.

¹⁸ Troy Senik, *Who Killed California?*, Nat'l Affairs, Fall 2009, at 60, available at http://www.nationalaffairs.com/doclib/20091229_Senik_Fall09.pdf

4.5% discount rate.¹⁹

As we will see, the size of the shortfall reflects the size of the promised pension benefits. Those benefits in turn reflect an inherently political process by which total wages are allocated between current pay, funded through the current budget and necessarily in competition with other demands on the budget, and future pension benefits, the budgetary impact of which can be put off into the future by, among other techniques, the choice of the return assumptions and simple underfunding.

Popular preferences for low taxes and high services may be sustainable—or at least deferrable—during times of economic growth. When recession comes, however, a combination of increased demands on the public fisc and lower revenues renders the fiscal situation more difficult, sometimes impossible, to sustain under previous assumptions. In the face of that reality, the hard choices of public policy—the need to allocate the burdens of the crisis among higher taxes, lower services and reduced prospective pension benefits to stem the fiscal tide, and how should those burdens be structured—follow directly and inextricably.

The timing of when political actors must confront their past promises has special bearing on the question of pension funding shortfalls. Because of the coincidence of macrocosmic difficulties and pension funding shortfalls, at precisely the time when voters employed in the private sector see their pensions cut or eliminated as a result of difficult economic times, the promised benefits from public pension plans made in a previous era come due. In effect, voters are asked to pay more for public employee benefits that they are not getting in their own jobs.

C. The Political Economy of Unfunded Benefits

To understand how we have arrived at a moment of crisis, it is important to understand the incentives of the parties that created the liabilities that are at the heart of the crisis. As does every participant in the labor market, government employees seek the best compensation for their services. That compensation typically comes in the form of a combination of current wages and deferred pension benefits.

¹⁹ Joseph Nation, *Pension Math: How California's Pension Spending is Squeezing the State Budget* 27-28 (Stanford Institute for Economic Policy Research, 2011). The discount rates reflect the assumed investment return on amounts contributed, ranging from the lowest rate, which reflects the return on Treasury instruments, to the highest rate, which is slightly higher than estimates of the largest funds' investment returns over the last 20 years. The arguments in favor or against each level of return are discussed in id., at 10 -17.

Generally, employers and employees should be indifferent between net-present value equivalents in their immediate distribution (wages) versus deferred distribution (pensions).²⁰ Given that general preference, the idea that the Constitution should protect one element of that compensation at the direct expense of the other appears nonsensical.

That indifference is a general proposition, absent other considerations. But resolving labor and employment negotiations through optimistically funded or even unfunded increases in pensions rather than through increases in wages has attractive features for both employers and therefore for employees, that are grounded in the familiar political economy of public employment. Increases in compensation through wages must be funded currently, with the result of displacing other competing demands on the government whether by using current tax revenue or the government's borrowing capacity. A responsible public official may then be forced to consider strikes associated with the provision of important government services, like schools and public transportation. And in their evaluation of such a strike, the public official will also realize that the voters may be badly hurt by a strike— working parents may not have alternative day care if the schools are closed, and alternative transportation to work may not be readily available if public transit is shut down, etc. For that reason, or more generally, the public may also support, politically, the provision of the compensation public employees seek since for them it trades off immediate salient costs against future costs. In contrast to present compensation, then, future promises of pensions resolve negotiation impasses in the short-term, without tapping the immediate budgetary constraints facing the public officials in same time horizon and without angering the electorate.

The consequence of promises made in good times coming due in hard times is at the core of what the political branches' fiscal policy-making apparatus must confront. When the promises made in an earlier time do not match the funds available in the present, public officials have two options. First, they can honor the pension commitments by raising taxes, taking on further debt, or eliminating other services. Second, the officials can renege on those commitments via, for example, bankruptcy (if a municipality rather than a state), con-

²⁰ For present purposes, we ignore rational reasons for employees to discount future benefits, especially when there is a vesting requirement, for example, when current employees do not expect employment to last longer than the vesting period. We also ignore employee risk aversion. As will become apparent, it does not change the outcome of the analysis. For significant and important exceptions, see Part II.B.2, *infra*.

tract renegotiation, litigation, or simply default.

The first option is not attractive. During times of economic recession and in the face of already high leverage, these options may be politically and economically unsavory; many of the state’s most expensive non-employment services—health care, welfare support, unemployment insurance, etc.—experience their most critical demand during a recession. And politically, there may be little enthusiasm for more debt and fewer services to support previous pension commitments at a time when the differences between public and private pension benefits will be most salient to the voters.

The second option isn’t much better. The failure to honor that commitment can trigger a countervailing political concern, including public strikes or political opposition from government employees, their unions and sympathizers in the general public, as well as earning the ire of the public who is inconvenienced by strikes. Additionally, it may result in loss of experienced workers, who will fear a loss in overall compensation, and so cause an indirect cut in the quality of public services.

The choice between these two classes of options—raise taxes, or shed the liabilities—will have political consequences. Public employee unions are active participants in the political process, and so will have supporters within the executive department and the legislature. And, as noted, honoring what are perceived as overly generous pensions while cutting other services, raising taxes, or expanding debt will trigger outcry from voters who will bear the service cut-backs or tax increases. Perhaps more directly, either option will invariably require participation by the legislature, which may be a source of the fiscal tension in the first place.

The range of choices public officials, public employees and the public face in fact is broader and more blended than our presentation of the three-party tension created by a significant pension funding shortfall. But the simple account highlights two aspects of the public pension crisis that are key to understanding the institutional role of courts in resolving those crises: (1) the crisis is the consequence of the intergenerational dodge baked into the incentives of the negotiating parties, and (2) the policy process that will result in either the “increase revenues,” “reduce services” or the “pension default” options is, in all ways, irretrievably *political*, in the Weberian sense.²¹ Thus, judicial intervention in this space can run the risk of endorsing that intergenerational dodge by engaging directly with an inherently political, as opposed to more formally legal, process.

²¹ MAX WEBER, *POLITICS AS A VOCATION* (1919), *reprinted in* FROM MAX WEBER: *ESSAYS IN SOCIOLOGY* 77, 79 (H.H.Gerth and C. Wright Mills ed., 1991)

D. *Institutionalist Critique*

Because the tradeoff between increasing revenues, decreasing services and decreasing pensions is inherently political, it also necessarily requires a comparative institutional analysis: which branch of government is best equipped to address this unattractive task. In the traditional framework, those contending institutions are three: legislative, executive, and judicial.²²

The judiciary has a specific but, we will argue, extremely limited role, to play in so political a game. To understand why, consider two axes: (1) the democratic legitimacy of the institution, by which we mean simply the directness of the institution's accountability to the electorate; and (2) the institution's ability to gather the facts necessary to evaluate competing proposals to resolve the gap between revenue and expenditures. Figure A describes the interaction between those two axes, and locates several institutions within the resulting quadrants.

²² We can imagine a role for delegated authority to other institutions. See Peter Conti-Brown, *Direct Democracy and Fiscal Crises: The Problem of Too Much Law*, 7 DUKE JOURNAL OF CONSTITUTIONAL LAW & PUBLIC POLICY 43 (2012) (proposing a federal-state collaboration in creating ad hoc committees given state legal authority to analyze fiscal lawmaking and its contributions to fiscal impasse).

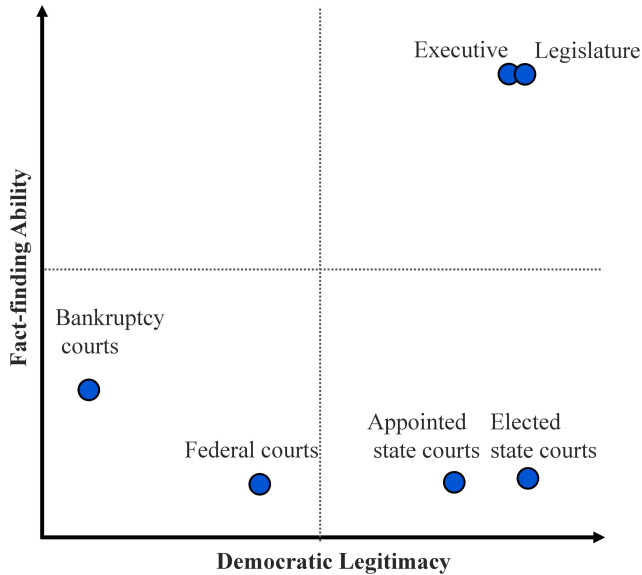
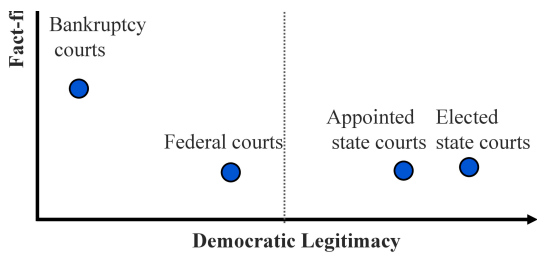


Figure A outlines the intersection of democratic legitimacy on the horizontal axis and institutional fact-finding ability on the vertical axis. The political institutions of the legislature and executive score the highest on both counts. The executive is essentially untrammelled in its fact-finding—its motivations may be entirely political, but it has access to relevant information through its own experts or outside consultants. Legislative hearings serve the same function. Democratic legitimacy is also high for both. While the entire legislative body may be divided by house at the state level, both state and local legislatures (in the form of city councils) face the electorate frequently, as do executive officials.

And then there is the judiciary. In the face of the fiscal mismatch between spending and revenues described above, the most competent institution is that furthest northeast on Figure A.²³ In cases where all

²³ If we could model the tradeoff between fact-finding and legitimacy, Figure A would include a curved frontier whose shape would reflect the marginal rate of substitution between units of fact-finding and units of legitimacy. Understating the

institutions are functioning, the courts will always be southern. Federal courts organized under Article III of the Constitution possess the least democratic accountability; lifetime terms are designed to provide federal judges protection from such accountability. To be sure, the local citizens vote for the President who appoints the judges. But historically (if not currently) the appointment of non-Supreme Court justices have rarely been a serious political issue, and indeed in some jurisdictions the President, in practice though not by law, yields that appointment power in part to Senators and with significant input by the local bar.²⁴ While more recently appointments of judges to the federal district courts and courts of appeal have become more political, the politicization of their appointment and confirmation do not lessen their independence from the political process once confirmed. Even when the relationship between the President and judicial appointment is more direct, as with nominations to the Supreme Court, the President faces a national electorate and a host of other policies for which he is accountable. To assume that lower-court judicial appointments would have significant electoral consequences is heroic at best; Supreme Court nominees may have greater salience, but even here their importance likely requires an issue that is expected to come before the court that is important to a large number of voters.

Elected state courts are closer to the polity and hence have greater legitimacy. But even there, the courts' institutional competence is constrained by courts' inherently limited fact-finding abilities. In common law traditions, the courts review only what is presented to them by the parties, whose discretion in choosing what to present is limited by the rules of evidence. And while adversaries in litigation can be quite thorough in their presentation of the law, they will always do so through the lens of litigation. Experts may be presented to the courts, but their choice and their testimony is shaped importantly

terms of the tradeoff and hence the institutions that might be on the frontier requires better theory and more careful analysis – both beyond our need for or ambition here.

²⁴ *Judicial Nominations and Confirmations*, UNITED STATES SENATE COMMITTEE ON THE JUDICIARY, <http://www.judiciary.senate.gov/nominations/judicial.cfm> (“The American Bar Association's Standing Committee on the Federal Judiciary also provides an evaluation of the professional qualifications of a judicial nominee”); *Nominations*, UNITED STATES SENATE, <http://www.senate.gov/artandhistory/history/common/briefing/Nominations.htm> (“Throughout the nation's history, appointments to judicial posts below the Supreme Court have generated little controversy...due in part to the large number of such appointments and to the tradition of "senatorial courtesy," which defers to the preferences of senators belonging to the president's party who represent a particular nominee's home state”)

by litigation strategy.²⁵ Legislatures and mayors/governors, whose inquiry is shaped by the policy problem at hand rather than the legal framing of the claim to which the policy problem may give rise, are simply better situated to gather information than courts.

Bankruptcy courts occupy a slightly improved situs for fact-finding purposes, but only slightly. Bankruptcy judges have more familiarity with the debt resolution procedure under the Bankruptcy Code. Theirs is a specialized docket, unlike courts of general jurisdiction. But that specialization is focused overwhelmingly on individual and corporate liquidation and reorganization. It is a contested question whether expertise with those kinds of restructurings increase bankruptcy courts' competence to evaluate fiscal policy, and if there are long gaps between episodes of fiscal crises, such judicial experience as may have been developed in one episode may dissipate by the next as a result of judicial turnover. Despite strong connections to the institutionalist critique and state-bankruptcy, we do not explore the connections between municipal bankruptcy and public pensions further.

Courts' deficits of democratic legitimacy is a problem in a variety of contexts,²⁶ but in crises this deficit is particularly pronounced. As Posner and Vermeule explain,

the basic problem underlying judicial review of emergency measures is the divergence between the courts' legal powers and their political legitimacy in times of perceived crisis. . . . [E]mergency measures [taken by the executive] can be "exceptional" in the sense that although illegal, or of dubious legality, they may nonetheless be politically legitimate, if they respond to the public's sense of the necessities of the situation. Domesticating this point and applying it to the practical operation of the administrative state, courts reviewing emergency measures may be on strong legal ground, but will tend to lack the political legitimacy needed to invalidate emergency legislation or the executive's emergency regulations.²⁷

²⁵ We do not intend this as a general slight on experts' independence. Rather, it is enough to note that experts differ in their point of view. This is observable to lawyers at the time experts are chosen, who in their roles as conductor of the litigation will decide whether they want to present a clarinet or an oboe.

²⁶ See, e.g., Kevin J. Mitchell, *Neither Purse Nor Sword: Lessons Europe Can Learn from American Courts' Struggle for Democratic Legitimacy*, 38 CASE W. RES. J. INT'L L. 653, 656 (2007) (corruption of individual judges as well as apparent judicial bias)

²⁷ POSNER & VERMEULE, *supra* note 1. As we discussed previously, the fact that a court may reexamine executive action after the crisis has abated provides a

Thus, even when the legal answer in the litigation is clear—that is, the executive’s decision to restructure public pensions is clearly legal or illegal—judicial intervention to announce the clear rule is troubling on the basis of democratic legitimacy alone.

As the second criterion in our schema suggests, the point is broader than the *political* legitimacy of the government’s actions in the face of fiscal restructuring. It is that the courts also lack *institutional* legitimacy in this circumstance. Interjections in this profoundly political space necessarily require interference with the very essence of democratic politics – the allocation of government attention and resources among competing claimants. As one court, in the context of Contracts Clause litigation put it,

Finding a [legislative action is forbidden by the Contracts Clause] has considerable effect. It means that a subsequent legislature is not free to significantly impair that obligation for merely rational reasons. Because of this constraint on subsequent legislatures, and thus on subsequent decisions by those who represent the public, there is, for the purposes of the Contract Clause, a higher burden to establish that a contractual obligation has been created.²⁸

This view reveals two central problems with courts’ fact-finding abilities. First, while courts will be offered the opinions of experts to aid them in their fact-finding and can ask parties to stipulate to uncontested facts, the very nature of fiscal facts are not prone to judicial resolution. Is a factually defensible expected rate of return for pension funds judicially determinable, even with the assistance of experts? Predictably, the experts chosen by the contending parties will differ significantly in their assessments of the “right” expectations. What about the tradeoff between future hiring and present pension payout rates measured either from the perspective of employment or service levels? And the consequences to public safety of each marginal tradeoff? The same might be true of the ultimate factual determinations of political actors, but the process that allows for a full airing of those determinations are much broader and more inclusive in the political branches than in courts. One does not, after all, have to demonstrate standing to participate in the political process.

check on marginally legal (or worse) executive actions taken in the heat of the crisis.

²⁸ *Parella v. Ret. Bd. of the R.I. Emps.’ Ret. Sys.*, 173 F.3d 46, 60 (1st Cir. 1999)

The second problem is related to the first. That an expert’s report will reflect the position sought by the party who chooses her does not suggest that the expert will be inventing facts in some venal attempt to mislead the court. Instead, the nature of fiscal facts is such that these “facts” are both predictions that unavoidably depend on assumptions and, as well, on political considerations. They are variable. They depend on judgments about the future. They reflect compromises. And they are thus better left to the political process.²⁹

E. *Justiciability and Political Dysfunction*

It would be tempting, then, to dismiss *any* judicial participation in the resolution of fiscal disputes. But two factors make that judicial participation inevitable, one legal and one pragmatic.

The legal factor is the doctrines of justiciability that govern the kinds of cases that the courts can or cannot entertain. For present purposes, we need not explore in depth these extensive doctrines.³⁰ The simple point is that, assuming personal and subject matter jurisdiction, courts—with only few exceptions—must resolve the cases that litigants have properly brought before them. A lack of institutional fit that does not exclude the matter from the courts’ jurisdiction does not relieve the court from its obligation to address the case. As we will see, however, it does counsel that the court’s limited institutional competence should result in the court restricting the extent of its intervention

One doctrine of justiciability, the political question doctrine, is of analogous relevance. The political question doctrine, in its iconic formulation, allows an exception to the general requirement that courts resolve cases before it when “there is a textually demonstrable constitutional commitment of the issue to a coordinate political department; or a lack of a judicially discoverable and manageable standards for resolving it.”³¹ So, for example, courts will refuse to meddle with the internal operations of the U.S. Senate, but will still adjudicate hot-button public policy disputes.

The resolution of fiscal policy disputes comes close to the second factor announced by the Court: “a lack of judicially discoverable and manageable standards for resolving” the issue. That said, courts adjudicate disputes between the government and its employees, citi-

²⁹ See text accompanying notes 9 to 18 for examples of “fiscal facts” that are more plainly political determinations.

³⁰ See ERWIN CHEMERINSKY, *FEDERAL JURISDICTION* CH. 2 (2012).

³¹ *Nixon v. United States*, 506 U.S. 224, 228 (1993) (quoting *Baker v. Carr*, 369 U.S. 186, 217 (1962)).

zens, bondholders, and other creditors all the time. The entire tax court system, reviewed by Article III courts, exists to adjudicate citizen challenges to fiscal policy (in the form of tax policy).

Thus, the question of whether unvested public pension commitments can be altered is not a political question in the constitutional sense of that term. Nor do we advocate raising the justiciability bar to preclude these kinds of disputes. Instead, we suggest a decision rule that might be viewed as a fellow traveler with the political question doctrine. The rule recognizes that, although justiciable, “the political question”—in the natural rather than the legal meaning of those words—points toward a need for the judiciary to resolve the fiscal dispute in a way that can be revised—indeed, rejected—by the political process should that process disagree with the judicial determination.

As we said earlier, there is also a pragmatic inevitability of judicial intervention in fiscal policy. Because fiscal crises are endogenous, the institutions with greater institutional competence, as we have defined it, are operating dysfunctionally. In other words, when the state is unable to bridge the fiscal gulf previous promises have created, the institutionally superior actors may find it very difficult to take advantage of their institutional superiority.

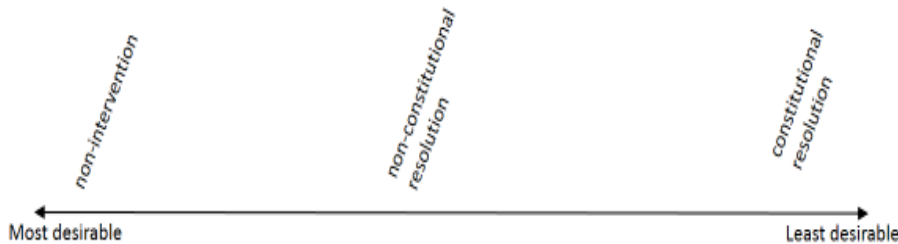
In those instances, the Komesarian charge to look for the “least bad” institutional option creates a role for limited judicial intervention. In effect, the crisis results in a change in state for the institutionally more competent politically accountable institutions. The fluidity of these institutions freezes, leaving them conceptually competent but practically frozen and therefore dysfunctional.

One of the primary reasons the judiciary retains its institutional incompetence even in the face of political dysfunction on the part of the conceptually more competent institutions, is the inability, *ex ante*, to determine whether the government’s actions that prompted the fiscal litigation occurred as an emergency response to bona fide crisis or as a political strategy to punish opponents. Bridges can be closed for different reasons. The difference matters, as we will see below, for the legal analysis. That the inability of other institutions to act creates the need for some judicial action does not alter the courts’ limited competence. Political actors—be they the institutions themselves, or those actors or factions whose interests are most affected by the resolution of the fiscal mismatch—can be expected to seek modification of fiscal commitments in both instances. Sophisticated political actors then can take advantage of the courts’ lack of institutional competence to further their own interest. Thus, courts must keep in mind their own limited competence when, predictably, they are drawn into the resolution of a fiscal crisis. More bluntly: courts shouldn’t have to

wonder whether they are used as a pawn in a political strategy, and should seek resolution of the dispute before them that cedes the political dispute back to the politicians.

F. *Where Legally Possible, Avoid the Constitution*

This central conclusion—that courts will entertain fiscal disputes so long as their jurisdiction is properly invoked even though they continue to lack the institutional competence to resolve them—does not end the comparative institutional inquiry. We still must evaluate the harder question: *what* the judiciary will do, not *whether* it will do it. The “what” is the commitment to treading lightly we have already introduced: when a court’s jurisdiction is properly invoked in a fiscal context, the response should be thoughtfully and thoroughly restricted. That the courts are put in a position where they must act does not improve their institutional competence. Rather, recognition of courts’ limited institutional competence helps delineate the self-imposed constraints that should define the court’s role in addressing fiscal crises. Figure B illustrates the continuum of the breadth of judicial intervention in response to litigation prompted by both a fiscal crisis



Of the three rough types of interventions available to courts when confronted by fiscal crisis litigation, the most desirable outcome in the abstract would be non-intervention. More precisely, perhaps, the ideal situation is where fiscal litigants elect not to invoke the courts’ jurisdiction at all. But the strategic character of fiscal crisis-related litigation makes this outcome highly unlikely. At least in the abstract, had the more competent institutions been able to act, the fiscal crisis could have been avoided in the first place. By the time of litigation, the courts may be the only institution left standing.

Having been put in this position, the court’s response must now reflect the limits of its institutional competence, even if it has, temporarily and in a limited way, “won” the institutional comparison vis-à-vis politically accountable institutions. Thus, at this point the most desirable outcome is that the court act such that the ball goes back to the political courts as quickly, and as unencumbered, as possible.

The reason for the superiority of non-constitutional resolutions is simple. Where the courts respond to fiscal crisis-based litigation with constitutional pronouncements, the self-induced freezing of the politically accountable institutions becomes permanent as the result of actions by a politically unaccountable institution. Subsequent efforts by the more competent institutions cannot undo what courts have done, regardless of whether these institutions would prefer to roll back the courts’ constitutional pronouncement and regardless of whether popular will supports that response. When the courts invoke the constitution to resolve a fiscal crisis, the court’s resolution can be reversed only through a constitutional amendment, a vastly more cumbersome process than the litigation that resulted in a petrifying outcome.³²

Figures A and B establish the three parts of our argument. First, courts are institutionally ill-suited to resolve fiscal crises. Second, because fiscal crises are endogenous to the political system, parties will seek judicial intervention only when there is a strategic or current inability to resolve the fiscal impasse through conventional political means. The third part follows from the first two. When courts are forced to intervene despite their limited institutional competence, and where the legal issue allows them the room, they should do so in a way that leaves the future resolution of the fiscal question to the political process. This “tread softly” decision rule reflects both the judiciary’s absolute institutional incompetence at making fiscal policy, but also the near impossibility, *ex ante*, to separate strategic litigation from absolute breakdown of the political process. The worst possible outcome is for the court’s to make a current pathology permanent.

II. THE HARD CASE: WHY THE CALIFORNIA RULE FAILS UNDER THE INSTITUTIONALIST ANALYSIS

The framework just described is illustrated by its application to litigation concerning the so-called California Rule, a judicial rule that

³² Kenneth P. Miller, *Constraining Populism: The Real Challenge of Initiative Reform*, 41 SANTA CLARA L. REV. 1037, 1067 (2001) (“The California rule, however, locks in initiative-made policies and thereby significantly undermines the legislature’s authority and flexibility”)

regards the statutes that describe the state’s public pension obligations as contracts protected by the Contracts Clause of the state and federal constitutions, even for benefits that have not yet accrued or vested. For example, a retiree who worked thirty years for the city’s fire department and is receiving monthly pension benefits as a result of that work is receiving vested benefits; a 30-year old fireman only has vested pension benefits tied to those years already worked. The projection of benefits in the future, tied to work not yet performed, are unvested. Most states regard pension obligations that have vested as protected by the Contracts Clause of the federal and California Constitutions.³³ What makes the California Rule unusual is its equivalent treatment of the expectation of pension rights that have not vested but which accrue at a specified rate conditional on the employee’s continued employment until vesting.³⁴

In an important and influential article, Amy Monahan carefully frames the debate surrounding the California Rule and provides a careful analysis of the legal and economic principles at stake. In the end, she criticizes the California Rule on legal and economic bases, and urges its abrogation.³⁵

If the legal critique succeeds—that is, if California courts had made basic errors of law in crafting and expanding the California Rule—there would be no reason to invoke the institutionalist framework we have described in this essay. Where the legal case is plain and within the obvious competence of the judiciary, a court has no need to defer to another institution’s competence to address the consequences of an endogenous fiscal crisis. We will see an example of this plain application in Part III.

But the legal and, relatedly, the economic issues are muddier than they seem. As a matter of law, the Contracts Clause jurisprudence leaves simply too much room to courts to determine the existence of contract, to interpret the contract’s language to determine its precise terms, and therefore to dictate the effect of governmental impairment on those contracts. And, in part based on the political economy described in Part I, and in part on factors considered in more detail below, the economic defense of the California Rule—the reasons why public employees actually might prefer a contract that locks in the rate at which future pension benefits accrue but allows the public employer to reduce future pension benefits, and thereby reduce current funding obligations, either by lowering employee’s wages or

³³ NEA COLLECTIVE BARGAINING & MEMBER ADVOCACY, NEA ISSUE BRIEF ON PENSION PROTECTIONS IN STATE CONSTITUTIONS (2004)

³⁴ Twelve states follow California. Monahan supra note 6 at 1071

³⁵ Monahan at 1032-1033

simply firing them—is stronger than it might seem at first blush. But even if economically rational in some circumstances, and this is still a stretch as we will see, the California Rule simply reifies the political economy pathology that gave rise to the endogenous fiscal crisis in the first place.

But while we regard the legal and economic contours of the California Rule as more complicated than do other critics, the institutionalist framework we offer here is as skeptical of the ultimate result. It is precisely *because* the law compels no clear result that the institutionalist framework must be invoked. In this circumstance, the determination of the contours of the state’s fiscal apparatus should be left to resolution by—indeed, foisted back upon—the more legitimate political branches. The judiciary should not be in the business of ending those negotiations by constitutionalizing the result. Any judicial resolution should, therefore, be readily reversible by the political process.

A. *The Legal Case for and against the California Rule*

The California Rule is open to at least two independent legal critiques: (1) “it runs contrary to the well-established legal presumption that statutes do not create contractual rights absent clear and unambiguous evidence that the legislature intended to bind itself”,³⁶ and (2) federal Contract Clause jurisprudence “holds that prospective changes to a contract should not be considered unconstitutionally impairments.”³⁷ Neither of these conclusions is inexorable; there are reasons why a court could conclude that California public employee retirement statutes do express clear evidence of contract; that the prospective changes referenced in federal Contracts Clause case law are different from pension obligations, especially as California has construed them; and that general principles of contract law are not offended by the peculiar terms of the pension contract as California courts have interpreted them.

We consider each argument in turn, but need not resolve which side has the best of the argument. Rather, we show that precisely because the questions are harder than they may at first appear, a court can and should be guided by an anti-constitutional decision rule that would facilitate pushing the resolution of the fiscal issue back to the political process. In this case, a “tread lightly” principle plainly leads to a decision not to constitutionalize the California Rule’s interpretation of the pension contract.

³⁶ Monahan, *supra* note 6, at 1032

³⁷ *Id.* at 1033.

1. Does a Contract Prohibiting Change in Prospective Accrual Rates Exist?

The Contracts Clause of the U.S. Constitution provides that “No state shall . . . pass any . . . Law impairing the Obligation of Contracts.”³⁸ But the prohibition against impairments is not absolute.³⁹ In one court’s articulation of the common test, “[i]n deciding whether such a demonstration [of unconstitutional impairment] has been made, the court must ask whether (1) a contract exists, (2) a change in law impairs that contract, and (3) the impairment is substantial.”⁴⁰ When the contract is based on state law, as is the case in the pension context, there are additional considerations. “A state law does not normally create contractual rights, but ‘merely declares a policy to be pursued until the legislature shall ordain otherwise.’”⁴¹

The first question in evaluating the California Rule is whether the statute that specifies the accrual and vesting of future pension benefits is “clearly and unequivocally expressed.”⁴² Put differently, assume what we will call the “hard case”: the statute does not directly state one way or the other whether a public employer can change the prospective accrual rate. Is the contract (statute) appropriately interpreted as allowing or prohibiting the government’s changing the pension accrual rate? Only if the facial ambiguity is properly interpreted as prohibiting prospective change do we reach the question of whether a contract has been substantially impaired.

Interpreting the statutory text is governed largely by state law. While some federal courts, including the U.S. Court of Appeals for Ninth Circuit (which covers California), have concluded that “federal rather than state law controls as to whether state or local statutes or ordinances create contractual rights protected by the Contracts Clause,”⁴³ the principles of contract formation are generally questions of state law. Indeed, as Monahan’s careful research has indicated, in the federal Contracts Clause jurisprudence, there are apparently

³⁸ U.S. Constitution. Art I § 10, cl. 1.

³⁹ Home Bldg. Y Loan Ass’n v. Blaisdell, 290 U.S. 398, 428 (1934).

⁴⁰ Mascio v. Pub. Emps. Ret. Syst. of Ohio, 160 F.3d 310, 313 (6th Cir. 1998).

⁴¹ Monahan, *supra* note --, at 1037, citing U.S. Trust Co. of N.Y. v. New Jersey, 431 U.S. 1, 17 n.14 (1977).

⁴² National R.R. Passenger Corp v. Atchison, Topeka & Santa Fe Ry. Co. 470 U.S. 451, 466 (1985).

⁴³ San Diego Police Officers’ Ass’n v. San Diego City Employees’ Retirement System, 568 F.3d 725 (9th Cir. 2009).

“no federal cases where a federal court ruled in direct opposition to a state court’s finding that a contract existed under federal law.”⁴⁴

The court reviewing a public pension contract entered recently—as opposed to the legal historical question of what a court should have done when the issue was first presented⁴⁵—must therefore look at the context of state law that animated the current parties’ contract negotiation. That legal context will include judicially-crafted law. And for almost a century, California has built up, and expanded upon, the notion that prospective contracts can be protected under the Contracts Clause. That century worth of law provides precedent for the conclusion that the pension statutes are contracts. In that sense, the California Rule’s very existence is self-validating: governments and employees entering into public pension contracts in the shadow of that Rule can be assumed to have relied upon its validity.⁴⁶ The same implication would not hold in jurisdictions where the Rule is not in place.

A California court, then, could resolve the statutory ambiguity that would otherwise would allow the absence of a contractual restriction on reducing the pension accrual rate for Contracts Clause purposes by reference to the parties’ assumed knowledge of the California Rule. This is not a circular argument; it would not apply to the majority of states that have not adopted the California view of prospective pension benefits, and it would not apply to the extension of the California Rule to new benefits. However, the argument that the existence of the California Rule allows a court to conclude that that the parties to an otherwise ambiguous contract intended to incorporate, *sotto voce*, pre-existing judicial precedent confronts an equiva-

⁴⁴ Monahan, *supra* n. 6, at 1045

⁴⁵ Monahan also makes an interesting historical discovery. In Monahan’s words, “the notion of pension rights as contractual rights became law through a single sentence of dicta in a California Supreme Court opinion describing pensions as a form of deferred compensation that are therefore ‘in a sense’ part of the contract of employment.” Monahan *supra* n. 6, at 1046. But the question is not whether a court in 1917 commented in passing that a statute of that era may have created constitutionally-protected contracts. Rather, the question is whether California courts have done so today with respect to the current state statute. The entire edifice of common law jurisprudence is built incrementally, where dictum in one case becomes the basis for a holding in another, not because it is binding but because it is persuasive. Indeed, there is an entire literature on the evolutionary dynamic of dicta becoming precedent. See, e.g., Judith M. Stinson, *Why Dicta Becomes Holding and Why It Matters*, 76 *Brook. L. Rev.* 219 (2010).

⁴⁶ That assumption is subject to challenge as an empirical matter. If early precedent, in effect, gave employees a bargaining edge that the parties then relied upon, we would expect to observe a change in the outcome of subsequent negotiations. Should a change not be observable, then the debate shifts to the implications of the stability in the contract’s terms in the face of important legal change.

lent but opposite argument. In light of the existence of the California Rule, the parties also might have chosen not to explicitly invoke it because they meant to allow the government to alter pension accrual rates prospectively. Without more, either is plausible, neither compelling.

2. Economics and the Hypothetical Bargain of the California Rule

Again, the hard case requires determining whether the parties intended to be bound by contract when the statute doesn't explicitly declare that intention. Part of that analysis, then, is whether the contract makes economic sense: that is, whether the parties intended for the future accrual schedules associated with pension benefits to be included as part of the overall public contract. The California Rule interprets the public employee contract as prohibiting the employer from changing the rate at which future pension benefits accrue, but leaves the employer free to lower the employees' wages, reduce other benefits or simply fire the employee, thereby ending all pension accruals. Monahan frames the economic criticism of interpreting the public employee employment contract in this way: As Monahan writes, the California Rule

appears to create inefficiency, in that it fixes in place one part of an employee's compensation. Under existing law, states can terminate employees, lower their salaries, and change their fringe benefits absent explicit agreements to the contrary. Yet California courts have held that even though the state can terminate a worker, lower her salary, or reduce her other benefits, the state cannot decrease the worker's rate of pension accrual as long as she is employed. This framework can be welfare reducing. Given the option, an employee may prefer to accept lower future pension accruals in return for avoiding termination or a reduction in current compensation, but such deals are hard to accomplish in a system that protects the right to future accruals. It should also be noted that the protections the California Rule appears to offer are illusory, given that it simply forces a state that needs to reduce costs to do so in some area other than pension accruals—for example, through layoffs or salary reductions. Viewed holistically, the California Rule simply does not protect employees'

economic interests, and in some cases the rule may even harm the interests of the very employees it is meant to protect.⁴⁷

This critique is straight-forward and intuitive. Why would employees seek to structure their compensation in this way?

We think there are at least three reasons why the California Rule might reflect the best bargain that employees and the state could secure, but this nonetheless counterintuitive result depends critically in each case on assumptions about future circumstances. First, the probabilities that modify each likelihood (i.e., what are the odds that in the absence of any restriction the state either would terminate the employee or adjust the rate of future pension accruals), given the costs to the state of pursuing each option, may encourage employees to push harder for pension protections than termination protections. If non-contractual costs make termination unlikely, the employee may trade off formal employment protection for contractual protection of future pension benefits.

Second, it may be easier for employees to get a new job if terminated even in a recessionary environment than to replace favorable pension accruals under a defined benefit pension plan. Given the decline in defined-benefit pensions in the private sector, there may be no substitutes for existing pensions when the substitute is needed even if alternative employment can be found.

Finally, and perhaps most convincingly, the political economy of public employee negotiations may make it more desirable for the state to substitute sufficient future compensation through increased pension accruals for current wages, that the tradeoff between current wages and future pension accrual will be favorable to the employee even if the employee may be terminated before any pension rights vest.

This last point, which is the most plausible, builds on the political pathology associated with public employment negotiation discussed in Part I: increases in current wages displace other government benefits that will disfavor some current voters and public worker strikes will seriously inconvenience many voters, in both cases to the disadvantage of current political incumbents. Thus, elected officials will be eager to trade future pension benefits for current wage increases at a rate that favors the employee. Indeed, it is this pathology that endogenizes a fiscal crisis. Put differently, the hypothetical bargain between current elected officials and current employees will reflect the

⁴⁷ Monahan *supra* note 6, at 1033.

gains to both sides from imposing costs on future elected officials who will have to confront the results of overpromising and underfunding future pensions, and future taxpayers who will have to pay for it. In this analysis, the resulting employee-friendly rate of substitution between current wages and future pensions makes up for the risk that an employee will be terminated.

a. *The Probabilities of Termination versus Pension Adjustment With No Contractual Guarantees*

The first indication that employees may prefer future compensation at the expense of present compensation is that the probabilities for each outcome may be different. If the employer faces no penalty in adjusting future pension promises, the cost to the employer for doing so may be lower than the cost of layoffs. These can be costly to a state employer because they mean the employer produces less of the particular government service for voters—even if terminated employees are replaced by less well paid and pensioned employees. The employer must retrain replacements, and the replacements will be less experienced and may be less talented than the employees who are laid off. The result is that the political actors may face costs associated with the layoffs, some immediately, including the political costs associated with the drop in services.

On these assumptions, adjusting prospective pensions may impose only the cost of increased difficulty in employee retention—some employees may quit, although that prospect is reduced in times of fiscal crisis because the crisis typically is associated with poor general economic conditions (which, of course, reads back on the employee’s assessment of the risk and cost of being laid off in the first argument). Even if the employer reduces future pensions entirely—as many private employers have done⁴⁸—such elimination is unlikely to be the equivalent of direct terminations. Only a percentage of employees will quit over the change in pension benefits. For the public employer, the budgetary benefit can be expected to come with a smaller impact on services valued by voters.

In some circumstances, a rational employee might want to roll those dice. She might reason that the government employer will lay off x percent of its employees y percent of the time, and that her individual risk of layoff is xy . The employee might also reason that, historically, xy has been very low. She might also suspect that, absent

⁴⁸ Daniel Gross, *Bye-Bye Pension!*, SLATE (Jan. 27, 2006, 4:17 PM), http://www.slate.com/articles/business/moneybox/2006/01/byebye_pension.html

stronger guarantees, the employer is likely to adjust pensions a percent of the time for 100% of its employees. And given the costs to the employer of such adjustments and employee's discount of the lost future pension benefits, $a > xy$, potentially by a significant margin. A rational employee could therefore want to avoid the greatest loss of compensation, adjusted for probabilities, and that would point toward guaranteeing the rate of future pension accruals even if those accruals remain subject to being terminated before vesting. In the end, however, the plausibility of the claim that employees may prefer the risk of layoffs to that of a reduced rate of future pension accrual depends on the *ex ante* probabilities.

b. *Substitution Costs Associated with Each Form of Compensation*

A second reason why rational employees might accept the combination of a guaranteed rate of future pension accruals even if an employee could be terminated before benefits vest is the employees' relative substitution costs—the costs of being forced to find a new job compared to the availability of similar pension benefits in other employment. That comparison may favor guarantees for prospective payment over guarantees of current employment. During years of employment, a terminated employee can seek reemployment in the labor market. The costs of doing so depends on the availability of alternative employment and the substitute wage. The likelihood of replacing a defined-benefit pension, on the other hand, is quite low in today's economy; the number of defined benefit plans has dropped significantly in the private sector. In 1990, defined contribution plans and Individual Retirement Accounts (IRAs) totaled \$1.5 trillion, and private defined benefit plans approximately \$1.6 trillion. Almost all of the subsequent growth in retirement assets has taken place in defined contribution plans and IRAs (\$9.2 trillion in total by 2010), rather than in private defined benefit plans (\$2.2 trillion by 2010). Moreover, the remaining defined benefit plans were increasingly in the public sector.⁴⁹

⁴⁹ The data comes from the Investment Company Institute, 2011 Investment Company Fact Book 101 fig.7.2, 102 (2011), available at http://www.ici.org/pdf/2011_factbook.pdf; David Crane, *Traditional Pension Plans Can Still Work. Really*, BLOOMBERG (June 24, 2013), <http://www.bloomberg.com/news/2013-06-24/traditional-pension-plans-can-still-work-really-.html> (“These traditional retirement benefits have been disappearing in

The employee's utility function extends presumably over her natural life: if the rational outcome is to maximize that function, then an economic assessment of the California Rule—the foundation for the hypothetical contract assessment of the constitutionally protected contract's interpretation—must pay attention to likely substitution costs to the employee of *both* termination of employment and adjustment/termination of future pension benefits. It is easy to imagine that function maximized for prospective pensions, particularly if (1) the likelihood of pension adjustment absent guarantee is higher than termination; (2) the likelihood of termination does not go up materially as a result of pension accrual guarantee; (3) the availability of the alternative employment is high; but (4) the alternative for comparable post-retirement compensation is low. Again, the plausibility depends on the expected probabilities.

c. The Public Employee Bargaining Pathology

The foregoing analysis is essentially a possibility analysis. Depending on the coefficients assigned to each variable, employees might or might not favor guaranteed pension accrual rates over increased wages. But the difficulty of the analysis for present purposes is that over time the value of the coefficients will change with economic and labor market conditions. For the hypothetical bargain interpretation to support constitutional protection of future pension accrual rates, the employees and the government employer's preference must remain constant, because constitutional protection serves to petrify the labor contract. There is, however, one explanation for why the parties might select the California Rule as a matter of preference that is far less sensitive to changing economic conditions: the political economy pathology of public employee bargaining.

Part I developed the political economy of public employee bargaining, and we won't entirely recount those points. It is sufficient to note only that the pressures and incentives of negotiating employees and public officials point very strongly toward structuring compensation so that paying that compensation will be somebody else's problem. Thus, at the time of negotiations, it may be in all parties' interests—the employees, the elected officials and the general public—to defer the hard choices until a later point when at least the elected officials and the electorate may be different. In other words,

the private sector...yet defined-benefit plans remain the dominant form of pension for state- and local-government employees")

the easy resolution to a thorny current fiscal problem is to make it the problem of future politicians, future employees, and future citizens. This phenomenon is the central factor in endogenizing fiscal crises: they result importantly from political system failures.

And here is the central irony in the California Rule. Employees may prefer pension protection over current wages, but this preference is highly sensitive to the fact that elected officials' preferences cause them to impose a high discount rate to future compensation for political as opposed to fiscal reasons. Thus, employees may well prefer the California Rule, but only because elected officials, in effect, are willing to pay so much more in future, but uncertain, pension benefits that they outweigh what would be available in certain current wages and job protection. The result is that the most plausible hypothetical bargain analysis of the California Rule results in constitutionally protecting the very political pathology that endogenizes fiscal crises in the first place.

3. The Impairment Requirement

The legal analysis does not end, however, with the determination that a contract with the terms reflected in the California Rule exists; to violate the Contracts Clause, the governmental action—here the reduction of future pension accrual rates—must also substantially impair the California Rule contract. And it is this last step⁵⁰ that provides the foundation for applying the institutionalist framework we develop in this essay. Whether an impairment is “substantial” is as open-ended an inquiry as it sounds. But a common conclusion is that an impairment is *not* substantial if it is “justified by a significant and legitimate public purpose” and is “both reasonable and necessary to fulfill such public purpose.”⁵¹

The public purpose exception is the vehicle by which a court can recognize its institutional incompetence in the fiscal policy-making space and therefore reach a conclusion that can be reversed in the political process, even if courts have been reluctant to invoke the exception historically. A court can—and we argue, should—determine that responding to an endogenous fiscal crisis satisfies the public purpose requirement and that reducing the level of prospective pension under-

⁵⁰ Again, the actual analysis separates the substantial impairment question into two: was there an impairment, and was it substantial? Because there is no question as to impairment, we collapse the two questions into one.

⁵¹ *Id.* (citations omitted).

funding is an appropriate means to address that purpose.⁵² This position would be buttressed by the frank acknowledgment courts are institutionally unsuited to resolving fiscal crises by removing that resolution from the political arena by constitutionalizing it.⁵³

For these reasons, we think the legal case against the California Rule is strong; but in jurisdictions where the public pension commitments were entered in the shadow of such a rule, the legal case in favor is, if not compelling, is also not weak. Resolving the interpretive question that underlies the California Rule is hard, particularly where the Rule has been in place for some time, and so may have been part of the negotiating context. We argue that this very difficulty, in the context of fiscal crises, points toward resolution by a determination that the impairment is justified by the public purpose exception; the alternative is to reify the political pathology that created the crisis. If the electorate disagrees, it can fire the officials who changed the law to impair the contract in the first place. An alternative ruling—that the change in law is unconstitutional—is essentially protected from democratic review.

III. THE EASY CASE THE COURT GOT WRONG: SAN JOSE AND THE APPLICABILITY OF THE CALIFORNIA RULE

Not all questions of contract interpretation in the public employment context are hard cases. The most obvious easy case is the one where the public employee has already performed the work associated with a specific pension commitment. That is, a retiree on a pension has no further work to do; one who has worked for ten years has already accrued future pension benefits based on those ten years of service. In these cases, the pension rights are “vested,” and not subject to future alteration without violating the Contracts Clause.

But there is another category of easy cases that do not require deep institutional analysis. That easy case is when the contract—in the form of the city charter and related documents—explicitly re-

⁵² Whitney Cloud, *State Pension Deficits, the Recession, and A Modern View of the Contracts Clause*, 120 YALE L.J. 2199, 2209 (2011) (Although allowing legislatures to use financial downturns as justification for modifying state contracts is risky, the effects of the Recession on pension deficits justify Contract Clause exception for Colorado’s pension modifications)

⁵³ See Peter Conti-Brown, *Is the Federal Reserve Unconstitutional? And Who Decides?*, LIBRARY OF LAW AND LIBERTY (Sept. 1, 2013) <http://www.libertylawsite.org/liberty-forum/is-the-federal-reserve-constitutional/> (summarizing the doctrine of “equitable discretion” that prevents a court from reaching a conclusion on a case that is otherwise justiciable)

serves the right to modify prospective pension commitments. In that case, the contract is clear: the terms allow for this kind of modification, and there can therefore be no impairment, substantial or otherwise. This is in the first instance pure contract law; the case is resolved before the court reaches Contract Clause analysis.

And yet, this case is worth exploring both because it is under active litigation in one of the most important examples of municipal pension crisis resolution, and because the trial court got the easy case exactly wrong. This Part briefly outlines the legal challenge of the efforts underway in San Jose, and how the city council, mayor, and voters sought to restructure their pension obligations consistent with the law—including the California Rule. It also outlines the December 2013 opinion of the Santa Clara County Court that found the city’s efforts violated the California Rule.⁵⁴ We explain how the court got it wrong, and why this is an easy case. We then explain that, even if one disagrees with our conclusion that the San Jose case is easy, the case nonetheless perfectly illustrates the dangers of constitutionalizing the fiscal policy-making apparatus. We do not offer a complete legal analysis of the issues involved in the case as framed by the Superior Court; for our purposes it is sufficient to show how the case illustrates why the judiciary is so ill-suited to fiscal policy-making, even in a crisis.

A. *San Jose’s Measure B*

Beginning in 2008, the city of San Jose—the capital of Silicon Valley, as it bills itself—faced a looming fiscal crisis. The crisis had not yet broken: that is, the city had not declared any kind of fiscal emergency.⁵⁵ But there was reason for the city to be nervous. In a single year, the city’s two retirement funds—one created by the city’s charter to provide pensions for its public safety employees (predominantly police and fire) and the second for the rest of its civilian employees—lost \$1 billion.⁵⁶ With the recession, the tax base shrank while the pension demands, with benefits and discount rates determined during rosier economic periods, stayed fixed and even expanded.⁵⁷

The city’s first response was to eliminate jobs and reduce city

⁵⁴ *San Jose Police Officers’ Association v. City of San Jose*, No 1-12-CV-225926 (tentative decision, filed December 20, 2013) (hereinafter “San Jose Police”).

⁵⁵ CITY OF SAN JOSE, FISCAL AND SERVICE LEVEL EMERGENCY REPORT (2011).

⁵⁶ *Id.* at 46.

⁵⁷ *Id.* at 52-54

services.⁵⁸ But the city, led by Democratic mayor Chuck Reed, also instituted a fiscal reform effort meant to place San Jose on stronger fiscal footing for the foreseeable future. The plan, which became the “Sustainable Retirement Benefits and Compensation Act,” and known generally as “Measure B,” was designed by the mayor and his advisers, adopted by the city council, and ultimately placed before the city’s voters for approval. On June 5, 2012, 70 percent of this overwhelmingly Democratic city approved the fiscal measures. The political affiliations are relevant only to highlight that San Jose was not a hotbed of anti-union sentiment.

Measure B included substantial changes to the city’s fiscal policies, but also included findings of legislative fact. Among other conclusions, the voters determined that “[t]he City’s ability to provide its citizens with Essential City Services has been and continues to be threatened by budget cuts caused mainly by the climbing costs of employee benefit programs, and exacerbated by the economic crisis.”⁵⁹ The voters also concluded that resolution of the looming fiscal crisis on the back of reduced services would “endanger the health, safety and well-being of the residents of San Jose.”⁶⁰ Even excluding the consequences to the city’s residents, the voters, by approving Measure B, also concluded that “[w]ithout the reasonable cost containment provided in this Act, the economic viability of the City, and hence, the City’s employment benefit programs, will be placed at imminent risk.”⁶¹

After determining these fiscal facts, Measure B proposed sweeping restructuring of how the city would compensate its employees. Some of its details are worth summarizing to illustrate how political and technical they are. New employees would be placed in a lower-cost retirement plan that required 50 percent contribution by the employees themselves, up from roughly 25 percent under the previous plan.⁶² Any defined benefit plan had a retirement age of 60 for public safety employees, 65 for other employees (up from 50 years and 25 years of service and 55 years, respectively),⁶³ with the option to retire

⁵⁸ *Id.* at 25-26.

⁵⁹ Sustainable Retirement Benefits and Compensation Act, SAN JOSE, CAL., CITY CHARTER art. XV, § 1501-A.

⁶⁰ *Id.*

⁶¹ *Id.*

⁶² Sustainable Retirement Benefits and Compensation Act, SAN JOSE, CAL., CITY CHARTER art. XV, § 1512-A (2013).

⁶³ Sustainable Retirement Benefits and Compensation Act, SAN JOSE, CAL., CITY CHARTER art. XV, § 1508-A (2013); *San Jose’s Pension Problems*, OFFICE OF MAYOR CHUCK REED (Sept. 9, 2012), <http://www.sanjoseca.gov/index.aspx?nid=2200#1>.

earlier with reduced benefits. Changes in the accrual rate provided that defined-benefit pensions could not exceed 2 percent of the employee's salary per year of service, with a maximum benefit of 65 percent. Under the previous system, the accrual rate for defined-benefit pensions for police officer was 2.5% per year for the first 20 years of service and 4% per year for every year thereafter, with a maximum benefit of 90%. The accrual rates for firefighters was roughly the same; for non-public safety employees, the accrual rate was 2.5%, with a maximum of 75%.⁶⁴

Again, these sweeping changes only applied to new employees. For current employees, Measure B gave the option of contributing more to keep the retirement plan that applied to them at the time of passage to ensure adequate funding, or to opt into a less generous prospective plan. Under the first option, the current employees could pay for the unfunded liabilities by contributing 4 percent of their salaries (with an additional 4 percent of their salaries added per year) until either the underfunded liabilities were covered, or the employees were paying 16 percent of their salaries, whichever came first. Under the second option, current employees kept benefits already vested, but would accrue in the future at a much lower rate prospectively, and have a higher retirement age.⁶⁵

Retirees' benefits would remain largely untouched. Measure B's only change to existing retiree benefits came in the form of an additional power to the City Council that would allow the Council to temporarily suspend retiree Cost of Living Adjustments during a fiscal emergency.⁶⁶ Measure B also eliminated "bonus" pension checks,⁶⁷ and prohibited the City Council from enhancing retirement benefits without city approval.

Immediately after Measure B was approved by the City and the voters, several employees, retirees, and public employee unions sued under various causes of action. We will focus here only those related to the Contracts Clause (and its California counterpart, the Impairment of Contract clause in the California Constitution).

⁶⁴ *San Jose's Pension Problems*, OFFICE OF MAYOR CHUCK REED (Sept. 9, 2012), <http://www.sanjoseca.gov/index.aspx?nid=2200#1..>

⁶⁵ Sustainable Retirement Benefits and Compensation Act, SAN JOSE, CAL., CITY CHARTER art. XV, § 1506-A(b) (2013).

⁶⁶ Sustainable Retirement Benefits and Compensation Act, SAN JOSE, CAL., CITY CHARTER art. XV, § 1510-A(a) (2013).

⁶⁷ "Bonus" pension checks occurred when the investment performance of the allowed it to remain fully funded after a bonus of the excess investment returns that year was paid to retirees. The San Jose court recognized that such bonus payments were unsound: if the City paid out the excess returns in good years, it would be short of funds in bad years, with the dynamic driving the fund into an unfunded status. *San Jose Police*, *supra* note XX at 22-27.

In its opinion on December 19, 2013, the Superior Court upheld several Measure B provisions, including those requiring voter approval of any changes to benefits and the elimination of special bonuses. But it held that future pension accruals vested at the time the employment contract is entered, as opposed to after the work associated with the benefits have accrued. The court recognized that the result was a contract that did not protect wages or employment, but protected only future accrual rates for employees that remained after layoffs. The court did not address the central interpretive question: whether the contract as the court construed it made any economic sense for the parties.

Both sides declared the court's decision a victory,⁶⁸ and Mayor Reed claimed that the negative results only “highlight[] the fact that current California law provides cities, counties and other government agencies with very little flexibility in controlling their retirement costs.”⁶⁹ The Mayor is wrong on both counts. The city lost the main legal event; the other challenges are a sideshow to the main event of pension reform. And the result is not compelled by California law, even given the California Rule. The result is to constitutionalize the political pathology that got San Jose where it was. Current elected officials and current voters were constrained by political decisions of prior officials to push the problem to future officials.

To understand the court's decision, and why the San Jose case is an easy one, we must understand the nature of the public employment contract the court construed. Unlike in other cases invoking the California Rule, San Jose's city charter explicitly reserves rights to the city to “amend or otherwise change” its retirement plans and to “repeal or amend” any retirement system. This ability to amend retirement plans is intended to shape the “contract” that would be subject to a Contracts Clause analysis. This strategy has been endorsed by California courts: “The modification of a retirement plan pursuant to a reservation of the power to do so [in a city charter] is consistent with the terms of any contract extended by the [retirement] plan and does not violate the contract clause of the federal constitution.”⁷⁰ In other words, the contract entered by the public employees included a right of amendment by the city; the city exercised that right; the contract was therefore not impaired, substantially or not. The reservation of rights makes this an easy case, far easier than where amendment

⁶⁸ Norimitsu Onishi & Rick Lyman, *Cut Salaries, Not Pensions in San Jose*, *Judge Rules* (N.Y. TIMES, Dec. 23, 2013), <http://www.nytimes.com/2013/12/24/us/a-mixed-ruling-on-san-jose-cuts.html>

⁶⁹ *Id.*

⁷⁰ *Walsh v. Bd. of Admin.*, 4 Cal. App. 4th 682, 700 (Cal. Ct. App. 1992).

clauses do not appear in the “contract” between the government and its employees.

The trial court disagreed, essentially without explanation. It initially rejected the plaintiffs’ whimsical arguments that the reservation-of-rights failed on its own terms, as it reserved the rights to the city council and not to the voters who ultimately approved Measure B. The court thought this an affront to democratic structure, but the argument is also inconsistent with the facts: the city council *did* approve Measure B; it was also approved by the voters subsequently.⁷¹

But the trial court’s main conclusion was that the sweeping language in *Walsh*—the case cited above—was limited case to its own peculiar facts.⁷² Those facts were indeed peculiar, as the case raised the unique situation where the California legislators transitioned from part-time to full-time status while, at the same time, completely redid district apportionments to make them consistent with the U.S. Supreme Court’s “one-person, one-vote” rule of equal protection.⁷³ But that is the problem with the *San Jose Police* court’s analysis: after concluding that *Walsh* provided a sensible rule of construction for “reservation-of-rights” clauses, it simply concluded that the “the last sentence of footnote 6” in the opinion meant that the application of the opinion should be restricted to its facts.⁷⁴ But applying old law to new cases is exactly the judicial function. The court should have at least made an effort to explain the applicability of the City’s reservation of rights, especially after the court had dismissed as unpersuasive the idea that the clause was facially illegal.⁷⁵

The court did not engage the nature of Measure B’s choices to allow employees to restructure their benefits under an option, did not differentiate—at all, even in passing—between accrued benefits and unaccrued benefits. Put most directly the court was not compelled to reach this result, and *Walsh* and the terms of the San Jose Charter invited it to credit the terms of the charter and shift the issue from the court room to the political arena.

The court’s error was in not doing so. This is an easy case: a reservation of rights may not preclude the creation of *any* vested rights subject to the Contracts Clause, but such a reservation surely puts bargaining parties on notice that prospective benefits are subject to change. The contract makes that likelihood plain. And so the court took for itself a choice better made by the political institutions, with-

⁷¹ *San Jose Police*, *supra* note XX at 10-11.

⁷² *Id.* at 11.

⁷³ *Walsh*, 4 Cal. App. 4th at 690.

⁷⁴ *San Jose Police*, *supra* note XX at 11.

⁷⁵ *Id.* at 10.

out ever engaging the issue.

The trial court's resolution of San Jose's Measure B is only the first round of the judicial process. The Court of Appeals and one would expect the California Supreme Court will have the opportunity to address both the contours and the wisdom of this judicial insertion into the fiscal policy-making process. We hope that their analysis—whether through the lens of the previously-announced public policy exception to the substantial impairment prong of the analysis, or through another means—comes to the conclusion we advance in this essay. The judiciary should avoid hamstringing cities, residents, and their representatives in the fiscal policy-making process in responding to an endogenous fiscal crisis. If the government has erred—if the results of their decision means an inability to recruit employees to provide the services the city's residents demand—let the politicians pay the price at the polls. Judicial policing of the efforts of current officials to respond to a current fiscal crisis erodes, and potentially destroys, the political accountability required to make fiscal policy work.

CONCLUSION

Fiscal crises are primarily if not exclusively political crises. When these political crises arise, judicial intervention can facilitate either continued dysfunction or, at best, temporary resolution. Given courts' institutional debilities in resolving fiscal disputes, and the difficulty in recognizing the line between genuine political institutional failure and strategic use of judicial intervention is so difficult, courts should tread very carefully.

This essay has tried to explain why. Institutionally, courts lack both robust fact-finding abilities and democratic legitimacy, making them institutionally less competent at resolving fiscal disputes. Less competent, but not altogether incompetent. When their jurisdiction is invoked, the result should be deference, even insistence, to politically accountable branches for further resolution; indeed, by declining to directly intervene the courts can sensibly insist that these institutions confront the crisis. Because fiscal crises are political crises that reflect shifting democratic priorities from one election to the next, judicial intervention that fixes the contours and incidence of fiscal crises across epochs removes the ability of political groups to resolve these concerns through a political process. The best judicial participation in fiscal disputes, then, is no participation at all. But if that option is made unavailable by invocation of the courts' jurisdiction, the next-best solution is judicial intervention that future political players can undo by statute. Constitutional pronouncements in fiscal crises

should only occur where there is no reasonable argument to be made on behalf of the non-constitutional determination. That is not the case with the California Rule, and it is decidedly not the case in San Jose where the terms of the City Charter makes the case easy.

This process will not be perfect, and may well create rent seeking opportunities for one or another politically powerful constituency. But that is the nature of the political process, and always has been. Destroying that process by judicial fiat merely crystallizes the political valence of a given epoch at the expense of shifting sentiment and temporary exigencies.