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## Finding a Port in the Storm: Constitutional Claims Find Protection Under the Fifth Amendment in Municipal Bankruptcy in *In re Financial Oversight & Management Board*

Mark Lammey

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2023]

FINDING A PORT IN THE STORM: CONSTITUTIONAL CLAIMS  
FIND PROTECTION UNDER THE FIFTH AMENDMENT IN  
MUNICIPAL BANKRUPTCY IN *IN RE FINANCIAL  
OVERSIGHT & MANAGEMENT BOARD*

MARK LAMMEY\*

I. SETTING SAIL: TAKINGS CLAUSE ISSUES FOR LARGE TWENTY-FIRST  
CENTURY CHAPTER 9 DEBTORS

In 2013, the City of Detroit filed what would become the largest Chapter 9 municipal bankruptcy to date in United States history.<sup>1</sup> In response to Detroit's first plan for reorganization, nearly every creditor group filed for protection of their claims against the city.<sup>2</sup> But these grim beginnings would give way to a remarkably effective and successful plan.<sup>3</sup> By December 2014, Detroit had reached a settlement with every creditor group *but one*; consequently, the bankruptcy court confirmed Detroit's plan, allowing the city to right the ship by adjusting \$7 billion of debt and reinvigorating the city's municipal services.<sup>4</sup>

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\* J.D. Candidate, 2024, Villanova University Charles Widger School of Law; B.S., 2014, University of Pittsburgh. This Note is dedicated to my wife, Aki, my constant source of motivation and support. Also, many thanks to my colleagues at the *Villanova Law Review* for their guidance, edits, and assistance in the writing process.

1. See Matthew Dolan, *Record Bankruptcy for Detroit*, WALL ST. J. (July 19, 2013, 6:32 AM), <https://www.wsj.com/articles/SB1000142412788732399380457861414173709204> [permalink unavailable] (describing the events surrounding Detroit's decline from the city known for its automobile and music industries to its eventual filing of "the country's largest-ever municipal bankruptcy case"); James L. Tatum III., *Detroit's Bankruptcy and Market Reentry*, 37 EMORY BANKR. DEV. J. 65, 70–74 (2020) (exploring the economic, financial, and social factors that led to problems for many United States industrial cities toward the end of the twentieth century and describing the issues Detroit faced leading up to the 2013 filing). Detroit, like many American cities, felt the effects of suburbanization, deindustrialization, and international labor competition throughout the latter half of the twentieth century. *Id.* at 70–71.

2. See *In re City of Detroit*, 524 B.R. 147, 159–60 (Bankr. E.D. Mich. 2014) (foregrounding its opinion by describing the situation at the outset of the bankruptcy). Detroit filed its first plan for reorganization in February of 2014 with "no approved settlement with any of its creditors." *Id.* at 160.

3. See Melissa B. Jacoby, *Federalism Form and Function in the Detroit Bankruptcy*, 33 YALE J. ON REG. 55, 56–57 (2016) (describing the combined effort of Michigan and several foundations that facilitated the ultimate success of the restructuring). Creditor groups, elected officials, the State of Michigan, and several private foundations all came together to effectuate the approved plan. *Id.* at 56. Jacoby indicates that the speed at which the bankruptcy progressed was "thought by many to be impossible." *Id.* at 57.

4. See *id.* (discussing the various sources of funding and financing, the amount of debt the city was able to adjust, and the remarkable speed with which

While the Detroit bankruptcy was unique for its size and notoriety, it did not greatly affect bankruptcy precedent.<sup>5</sup> One exception was on the issue of dischargeability.<sup>6</sup> In bankruptcy, one goal of the process is to give the debtor a fresh start, which often requires adjusting or discharging much of the debtor's debt.<sup>7</sup> Not all forms of debt can be discharged.<sup>8</sup> In the case of consumer debtors, unsecured loans and money judgments are forms of debt that can often be discharged or adjusted down in large

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the proceedings were completed); *In re Detroit*, 524 B.R. at 160 (explaining the turnaround in creditor support and enumerating the creditors that had not yet reached settlement at the time of confirmation). The only group that had not reached settlement with the city were creditors with claims for violations of constitutional rights. *Id.*

5. See Jacoby, *supra* note 3, at 59 (describing the Detroit bankruptcy as having "produced relatively little new doctrine"). The court held the "Michigan Constitution characterizes pension claims as contract rights" which allowed for their impairment in the plan. *Id.* at 59 n.22. While pensions were ultimately reduced, the cuts were mitigated by an influx of capital as part of the plan. *Id.* at 70. Pension plans received \$800 million from the state and private foundations as part of the bargain, something that will not likely be available in most municipal bankruptcies. *Id.* at 100 n.323.

6. See *id.* at 59 n.22 (discussing the doctrine resulting from the Detroit bankruptcy). The court held that pensions could be impaired through its state constitution interpretation, and "made new law on the dischargeability of civil rights and the nondischargeability of Takings Clause claims." *Id.*

7. See HENRY J. SOMMER & RICHARD LEVIN, COLLIER ON BANKRUPTCY ¶ 1.01[1] (16th ed. 2022) ("The Supreme Court has long and often stated that '[t]he principle purpose of the Bankruptcy Code is to grant a fresh start to the honest but unfortunate debtor'" which Collier also indicates allows "the ability to restructure their debts in certain circumstances" (alteration in original) (quoting *Marrama v. Citizens Bank of Mass.*, 549 U.S. 365, 367 (2007)); Michael D. Sousa, *The Principle of Consumer Utility: A Contemporary Theory of the Bankruptcy Discharge*, 58 U. KAN. L. REV. 553, 562 (2010) (describing the purpose and effect of a discharge in bankruptcy). One of the primary policy goals of the bankruptcy process is to provide relief to the debtor of their indebtedness. *Id.* With regard to individual debtors, the discharge is a "permanent injunction against any act to collect a discharged debt." *Id.* However, a discharge is not available for all types of debts. *Id.* at 568. A debtor who has behaved improperly may be denied a discharge altogether if they, for example, transfer or destroy their property within a year of filing for bankruptcy with an "intent to hinder, delay, or defraud a creditor." *Id.* Even if a debtor is able to receive a discharge, particular debts may be exempted from the discharge. *Id.* Congress has decided that, in some cases, the interest of the creditor in receiving full payment of a debt "outweigh[s] the debtor's interest in a complete fresh start." *Id.* See generally Eric W. Sleeper, *Discharge: Sections 727, 524 and 523*, 2 BANKR. DEV. J. 115 (1985) (discussing the sections of the Code dealing with the availability and effect of the bankruptcy discharge). Section 524 of the Code describes the legal effects of a discharge, chiefly it will "shield the debtor from any further personal liability on a discharge[d] debt by avoiding any judgments existing thereon and by creating a permanent injunction against any further effort to collect or recover on the debt." *Id.* at 120.

8. See Sousa, *supra* note 7, at 568 (discussing which debts are and are not dischargeable). 11 U.S.C. § 523 enumerates several categories of debt that cannot be discharged. *Id.* For example, income tax, student loans, and domestic support payments cannot be discharged. *Id.* at 568–69.

part.<sup>9</sup> However, secured loans are given much greater protection than unsecured ones.<sup>10</sup> If a creditor wants to receive a payout in a bankruptcy proceeding, it is often beneficial to find ways to make debt exempt from impairment.<sup>11</sup> With the financial incentive of being paid out in full, it is no surprise that creditors—and their counsel—typically seek out any protections for their claims that the Bankruptcy Code (Code) provides.<sup>12</sup>

The one group of creditors in the Detroit bankruptcy that did not reach settlement was comprised of those with constitutional claims against the city.<sup>13</sup> Within that group were individuals with civil rights claims

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9. See *id.* at 569 n.84 (“any debt not excepted by Congress in the Bankruptcy Code is presumed to be dischargeable.” (quoting *In re Butler*, 186 B.R. 371, 372 (Bankr. D. Vt. 1995))); Scott F. Norberg & Andrew J. Velkey, *Debtor Discharge and Creditor Repayment in Chapter 13*, 39 CREIGHTON L. REV. 473, 477 (2006) (stating that in 45% of cases with a proposed distribution, debtors proposed to pay less than 25% of unsecured claims).

10. See SOMMER & LEVIN, *supra* note 7, ¶ 1.07[5][e] (discussing the disparate rights of unsecured and secured creditors in chapter 13). “The protection afforded unsecured creditors is that the plan must provide for them to receive at least as much as they would obtain in a hypothetical chapter 7 liquidation and, if one creditor or the trustee objects, to receive their pro rata share of the debtor’s disposable income.” *Id.* “A secured creditor is entitled to retain its lien and receive payments equaling the present value of the secured claim.” *Id.*

11. See *Mission Prod. Holdings, Inc. v. Tempnology, LLC*, 139 S. Ct. 1652, 1658 (2019) (acknowledging that in a “typical bankruptcy” unsecured creditors “may receive only cents on the dollar”). The central issue in this seminal case dealt with the ability to reject certain types of contracts and the Code’s decision to treat such breaches as occurring pre-petition, thereby placing those creditors “in the same boat as the debtor’s unsecured creditors.” *Id.* at 1653; see also Sousa *supra* note 7, at 569 n.84 (explaining that the Bankruptcy Code requires “the complaining creditor to initiate an adversary proceeding against the debtor” to have a debt exempted from the discharge).

12. See *generally* 11 U.S.C. §§ 523, 727 (2018) (detailing the circumstances that allow claims to be exempted from discharge and outlining when the debtor can be denied a discharge, respectively).

13. See *In re City of Detroit*, 524 B.R. 147, 262 (Bankr. E.D. Mich. 2014) (addressing the objections of the creditors with constitutional claims). Several individuals had filed lawsuits against the city prior to the bankruptcy alleging violations of their First, Fourth, Fifth, Sixth, Seventh, and Fourteenth Amendment rights. *Id.* at 263; see also U.S. of Am. Br. in Resp. to Ord. of Certification Pursuant to 28 U.S.C. § 2403(a) at 2–3, *In re Detroit*, 524 B.R. at 147 (No. 13-53846), ECF No. 6664 (addressing the potential unconstitutionality of confirming a plan discharging civil rights claims). The brief laid out the objections of eight creditors; all of them had pending lawsuits against Detroit and its officials for violations of the Civil Rights Act. *Id.* at 2. The plan they objected to would have paid them 10–13% of the liquidated value of their claim. *Id.* at 3; Objection of Creditors at 2–3, *In re Detroit*, 524 B.R. at 147 (No. 13-53846), ECF No. 4099 (describing the civil rights violations within some of the pending lawsuits). This filing detailed the claims of four individuals. *Id.* The first individual claimed that Detroit and its officials had acted in a manner that substantially increased the risk of danger to their daughter, a police officer, who had been murdered. *Id.* at 2. The second individual claimed that he had been wrongfully convicted and served twenty-six years in prison, and that Detroit and its officials were involved in his wrongful conviction, in malicious prosecution, and hiding of evidence. *Id.* The last two, a professor and student, claimed that Detroit and its officials used excessive force and engaged in malicious prose-

(§ 1983 Creditors) and individuals with Takings Clause claims.<sup>14</sup> The bankruptcy court faced the unprecedented issue of whether a city could escape or minimize its liability for constitutional violations through bankruptcy discharge.<sup>15</sup> Ultimately, the court decided that claims brought by the § 1983 Creditors against the city were dischargeable.<sup>16</sup> However, the court found that the claims raised under the just compensation guarantee of the Takings Clause were not dischargeable by relying on the general proposition that the bankruptcy power is subject to the limitations of the Fifth Amendment.<sup>17</sup> The *In re City of Detroit*<sup>18</sup> court's decision to find Takings claims to be nondischargeable in Chapter 9 bankruptcies laid the

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cution resulting from an incident on a public street where the professor took photographs of a movie set. *Id.* at 3. Each group of claimant pointed to multiple constitutional amendments they alleged the City and its officials had violated. *Id.* at 2–3.

14. See *In re Detroit*, 524 B.R. at 267 (noting the details of the two Takings Clause claims). The first claimant had obtained a judgment against the city for an “ongoing Fifth Amendment Takings violation due to certain land use restrictions.” *Id.* The second claim was made by two creditors with pending suits against the city for just compensation. *Id.*; U.S. of Am. Br. in Resp. to Ord. of Certification Pursuant to 28 U.S.C. § 2403(a) at 3–8, *In re Detroit*, 524 B.R. 147 (No. 13-53846), ECF No. 6664 (discussing the procedural posture of the Takings claimants). The three separate claimants held claims for pending condemnation, pending inverse condemnation, and a final judgment for pretrial inverse condemnation. *Id.* at 3. The United States’ brief analyzed this group separately from the civil rights claims for purposes of determining the constitutionality of the plan. *Id.* at 4–9; see also U.S. CONST. amend. V (“nor shall private property be taken for public use, without just compensation”).

15. See *In re Fin. Oversight & Mgmt. Bd.*, 41 F.4th 29, 44 (1st Cir. 2022) (describing the court in the Detroit bankruptcy as the first federal court to “squarely address[ ] the question of whether the Fifth Amendment prohibits the discharge or impairment of claims for just compensation in bankruptcy” (citing *In re Detroit*, 524 B.R. at 269–70)), cert. denied 143 S. Ct. 774 (2023). On the issue of civil rights violation claims, no party had argued that such claims could not be impaired, so the First Circuit assumed without deciding that they could, suggesting that the violative nature of such an action is still unsettled. *Id.* at 44 n.6.

16. See *In re Detroit*, 524 B.R. at 265 (holding that impairment or discharge of the civil rights claims was not constitutionally barred). For a discussion of the rationale the court used in discharging the civil rights claim, see *infra* Section II.D.

17. See *In re Detroit*, 524 B.R. at 268 (holding that allowing the discharge of Takings claims would result in a constitutional violation because the Fifth Amendment mandates that “private property [shall not] be taken for public use, without just compensation” and because the bankruptcy power is subject to the Fifth Amendment, (alteration in original) (quoting U.S. CONST. amend. V)).

18. 524 B.R. 147 (Bankr. E.D. Mich. 2014).

groundwork for the current circuit split.<sup>19</sup> Three years later, the Ninth Circuit affirmed the discharge of a just compensation claim in the City of Stockton bankruptcy.<sup>20</sup>

In 2017, the Commonwealth of Puerto Rico began the arduous process of restructuring its debts through municipal bankruptcy, and in June of 2022, the First Circuit was also called upon to resolve this issue of whether the discharge of Takings claims was constitutional in *In re Financial Oversight & Management Board*.<sup>21</sup> Like the *In re Detroit* court, the First Circuit found that claims based on eminent domain and inverse condemnation could not be discharged in bankruptcy without violating the Constitution.<sup>22</sup> The court based its holding on the general proposition that Congress's bankruptcy power is subject to the limitations of the Fifth Amendment.<sup>23</sup>

This Note argues first that the mantra “the bankruptcy power is subject to the Fifth Amendment” came about by relying on inapposite precedent and is too rigid a rule to adapt to the changing landscape of Takings Clause jurisprudence. Second, this Note contends that the First Circuit's refusal to discharge Takings claims is logically inconsistent given recent Supreme Court precedent on the timing of Takings violations.<sup>24</sup> Finally, this Note asserts that as Takings Clause protections continue to evolve and expand, adherence to this mantra will allow unintended claimants to seek the safe harbor of the Fifth Amendment to prevent discharge of their claims.

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19. See *In re Fin. Oversight*, 41 F.4th at 45 (acknowledging that *In re Detroit* was the first federal court to analyze whether the “Fifth Amendment prohibits the discharge or impairment of claims for just compensation in bankruptcy” (citing *In re Detroit*, 524 B.R. at 269–70)). The First Circuit also identifies the issue as raised in the Stockton bankruptcy in the Ninth Circuit, deciding that “dissenting opinion” in that case was “more persuasive.” *Id.*

20. See *In re City of Stockton*, 909 F.3d 1256, 1266 (9th Cir. 2018) (holding that the Takings Clause is only offended if the creditor has actual property rights, thus allowing for the discharge of a just compensation claim in Chapter 9 bankruptcy).

21. 41 F.4th 29 (1st Cir. 2022), cert. denied 143 S. Ct. 774 (2023); see also *id.* at 29 (contributing to the growing circuit split over the dischargeability of constitutional claims based on the First Circuit's decision). See generally 48 U.S.C. § 2101 (2018) (referring to the Puerto Rico Oversight, Management, and Economic Sustainability Act (PROMESA); the act that Congress passed to facilitate the Puerto Rican bankruptcy that integrated much of language of Chapter 9 of the Code).

22. See *In re Fin. Oversight*, 41 F.4th at 37 (holding that the otherwise valid Fifth Amendment Takings claims that arose prepetition could not be discharged in bankruptcy without full payment of just compensation).

23. *Id.* at 42 (“The bankruptcy laws are subordinate to the Takings Clause.”); see also *United States v. Sec. Indus. Bank*, 459 U.S. 70, 75 (1982) (“The bankruptcy power is subject to the Fifth Amendment's prohibition against taking private property without compensation.”); *Louisville Joint Stock Land Bank v. Radford*, 295 U.S. 555, 589 (1935) (“The bankruptcy power, like the other great substantive powers of Congress, is subject to the Fifth Amendment.”).

24. See *infra* Section II.C (discussing the Supreme Court's reasoning and holding regarding the timing of federal Takings claims in *Knick v. Township of Scott*).

Part II explores the evolution of the Takings Clause, its historic application to bankruptcy law, and the current friction in modern large-scale municipal bankruptcies. Part III summarizes the facts and procedure leading up to *In re Financial Oversight*. Part IV details the First Circuit's reasoning and conclusions in the case. Part V critically analyzes the First Circuit's holding and raises potential issues that arise from treating Takings Clause claims differently than other constitutional violation claims. Finally, Part VI explores the impact this holding will have on future creditors in municipal bankruptcies and the difficulties that arise from a rigid interpretation of the Takings Clause.

## II. THE CALM BEFORE THE STORM: THE LONG HISTORY OF BANKRUPTCY AND THE TAKINGS CLAUSE

Bankruptcy processes can often operate in seeming contradiction to other areas of law. By allowing impairment and discharge of particular obligations, the Code allows a debtor to escape debts they would otherwise be contractually obligated to pay.<sup>25</sup> The Code allows for the adjudication of contested matters by a non-Article III judge, which has routinely come under constitutional scrutiny; the contours of bankruptcy jurisdiction are still a contested issue.<sup>26</sup> Finally, by getting involved in the collection and disbursement of property and money, bankruptcy has naturally produced debate about whether and to what extent the Takings Clause creates constitutional limits on its operation.<sup>27</sup>

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25. For a discussion on bankruptcy discharges, see *supra* note 7.

26. See Laura B. Bartell, *Stern Claims and Article III Adjudication—The Bankruptcy Judge Knows Best*, 35 EMORY BANKR. DEV. J. 13 (2019) (discussing the nuances of how bankruptcy judges are required to deal with proceedings outside their power). Bankruptcy judges are not appointed as Article III judges and thus do not have the power to hear certain types of claims that arise during the bankruptcy process. *Id.* Bankruptcy judges thus have the power to “hear and determine” certain claims closely tied to bankruptcy matters but are only permitted to “hear” others and must “submit proposed findings of fact and conclusions of law to the district court.” *Id.* The Supreme Court has repeatedly analyzed the constitutional limits of the power given to bankruptcy judges. *Id.* at 13–14.

27. Compare James Steven Rogers, *The Impairment of Secured Creditors' Rights in Reorganization: A Study of the Relationship Between the Fifth Amendment and the Bankruptcy Clause*, 96 HARV. L. REV. 973, 973–74 (1983) (arguing that Article 1, section 8 of the Constitution, the Bankruptcy Clause, gives Congress broad power to adopt laws to deal with the issues of insolvency and financial distress, allowing it to “disregard all manner of contractual and property rights of creditors and other investors”), with Julia Patterson Forrester, *Bankruptcy Takings*, 51 FLA. L. REV. 851, 856 (1999) (analyzing the extent to which the bankruptcy power is limited by the Takings Clause). Rogers identifies the prevailing belief that “the fifth amendment limits the extent to which secured creditors may be subjected to risk of loss due to restraint of their foreclosure rights.” *Rogers, supra*, at 977. He argues that such a position is constitutionally unsound and that other limitations in the Constitution “do not impose substantive limitations on congressional exercise of the bankruptcy power.” *Id.* at 998. Forrester believes that “the Takings Clause is a vital consideration in determining the treatment of secured creditors in bankruptcy.” *Forrester, supra*, at 857. Forrester points to the understanding of the drafters of the Bank-

For many, the hallmark of bankruptcy is the discharge; that is, upon consummation of a bankruptcy plan, creditors may not receive full payments of debts or judgments and are, instead, barred from attempting to collect those debts.<sup>28</sup> Regardless of the varied views on the wisdom of such a system, the current American bankruptcy system attempts to give individual debtors a fresh start and incentivize ailing businesses to restructure rather than liquidate.<sup>29</sup> The process necessarily means that some party is left worse off, typically the unsecured creditor.<sup>30</sup> This comes about partly because secured creditors—those whose debts are backed by collateral, often real property—cannot have their debts impaired below the value of that collateral.<sup>31</sup> Though the Code may augment the rights of some creditors, the Takings Clause has been a perennial watchman limiting bankruptcy's effect on private property.<sup>32</sup>

Given the current state of bankruptcy precedent—and popular notions about the protections of the Fifth Amendment—it may seem perfectly reasonable that Takings claims should survive the bankruptcy unimpaired.<sup>33</sup> However, there are strong arguments to the contrary, and the issue is not resolved by simply referring to the preeminence of the

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ruptcy Code that the Fifth Amendment does limit the impairment of property rights and legislative history suggesting Congress acts in deference to property rights for both policy and constitutional reasons. *Id.* at 859.

28. See 11 U.S.C. § 524 (2018) (noting the “[e]ffect of discharge,” which statutorily voids any judgments and acts as injunction against collection efforts for any debts that have been discharged by the bankruptcy court).

29. See SOMMER & LEVIN, *supra* note 7, ¶ 1.01[1] (discussing the goals of Bankruptcy). See generally Nathalie Martin, *Common-Law Bankruptcy Systems: Similarities and Differences*, 11 AM. BANKR. INST. L. REV. 367, 368–70 (2003) (discussing the differences between common-law systems of bankruptcy). The United States is unique for giving the debtor substantial freedom in deciding whether to pursue liquidation or reorganization. *Id.* at 368. Other countries have a more negative view of bankruptcy and are not nearly as lenient as the United States' system, thus the wisdom of having a system so amenable to restructuring is not universally accepted. *Id.* at 369–70.

30. See SOMMER & LEVIN, *supra* note 10, ¶ 1.07[5][e] (discussing the difference in treatment between secured and unsecured creditors in Chapter 13).

31. See *id.* ¶¶ 1.07[3][d][vi], [5][e] (describing the rights of secured creditors in different forms of bankruptcy). In Chapter 11 proceedings, secured creditors can retain the lien on the secured property and receive payments up to the present value of the allowed secured claim. *Id.* ¶ 1.07[3][d][vi]. In Chapter 13 proceedings, “[t]he secured creditor is entitled to retain its lien and receive payments equaling the present value of the secured claim, i.e., the value of the collateral.” *Id.* ¶¶ 1.07[5][e].

32. See Forrester, *supra* note 27, at 866 (“The Supreme Court has addressed the takings issue in the context of bankruptcy on several occasions, holding each time that the bankruptcy power is limited by the Takings Clause.”).

33. See *id.* at 911 (concluding that the inability to convey a security right that can survive bankruptcy may be such an important property right that “its abrogation would constitute an impermissible taking”). Forrester goes on to conclude that interference with the right of an owner to transfer land “would most certainly be an unconstitutional taking.” *Id.*



Fifth Amendment.<sup>34</sup> In Part II of this Note, Section A traces the history of the Takings Clause and how its protections have expanded over time. Section B explores how those protections have interacted with bankruptcy laws. Section C details the recent Supreme Court decision regarding the timing of Takings claims and their interaction with § 1983 civil rights claims. Lastly, Section D directly looks at the recent trio of federal cases making up the current circuit split.

#### A. *History of the Expanding Takings Clause*

The Fifth Amendment was originally a limitation on the federal government.<sup>35</sup> After the passage of the Fourteenth Amendment, the Fifth Amendment's guarantees were eventually applied to the states through incorporation.<sup>36</sup> While the Fifth Amendment's original purpose is debated, it was clearly understood to at least protect "direct, physical takings"—that is, condemnation of land.<sup>37</sup> In the late nineteenth century, the Supreme Court expanded the Takings Clause to allow compensation for physical invasions of property stemming from government action, like

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34. See *id.* at 873 (recognizing that the debate over the existence of certain property rights can be a normative one). While her discussion is aimed at the adjacent issue of secured property interests rather than Takings claims, Forrester acknowledges that some scholars believe that security interests should not be treated as property rights. *Id.*; Rogers, *supra* note 27 at 993 (arguing that it is incorrect to assume "that the takings clause or other fifth amendment principles provide an independent source of limitations on the substantive scope of the bankruptcy power"). Rogers believes that the bankruptcy clause stands alone as the limit on Congressional power in this area and "the constitutionality of a statute adopted under the bankruptcy clause depends only on whether that measure falls within the scope of the powers conferred by the bankruptcy clause." *Id.* at 998; see also *In re City of Stockton*, 909 F.3d 1256, 1261 (9th Cir. 2018) (characterizing a plaintiff's actions following an eminent domain taking as "waiv[ing] all of his defenses and claims to the property, except a claim for greater compensation"). The majority opinion held that the Takings Clause did not provide the plaintiff any protection because the "Takings Clause is only implicated in bankruptcy if the creditor has actual property rights." *Id.* at 1266. The Ninth Circuit chose to view the claims as a "contractual or statutory right for monetary relief" rather than a property right and consequently held that the debt could be constitutionally adjusted in bankruptcy. *Id.*

35. See *Barron v. Mayor and City Couns. of Balt.*, 32 U.S. 243, 250–51 (1833) (holding that the Fifth Amendment's declaration that private property shall not be taken for public use without just compensation was intended solely as a limitation on the federal government and "is not applicable to the legislation of the states").

36. See *Chi., Burlington & Quincy R.R. v. Chicago*, 166 U.S. 226, 238 (1897) (overruling prior precedent and incorporating the Taking Clause). "The legislature 'can no more take private property for public use without just compensation than if this restraining principle were incorporated into, and made part of, its state constitution.'" *Id.* (quoting *Sinnickson v. Johnson*, 17 N.J.L. 128, 146 (N.J. 1839)).

37. See Andrew S. Gold, *Regulatory Takings and Original Intent: The Direct, Physical Takings Thesis 'Goes Too Far'*, 49 AM. U.L. REV. 181, 183 (1999) (discussing the original conception of the Takings Clause in *Lucas v. S.C. Coastal Comm'n*, 505 U.S. 1003 (1992) and the disagreement on how it ought to be applied today with competing views as to its true intention).

flooding from a government-run dam.<sup>38</sup> However, in evaluating land regulation, the analysis originally proceeded under substantive due process and many land regulations were upheld under state police power.<sup>39</sup>

In 1922, the Supreme Court decided *Pennsylvania Coal Co. v. Mahon*<sup>40</sup> and held that a taking had occurred by operation of a state statute forbidding coal mining in certain areas, noting that “if regulation goes too far it will be recognized as a taking.”<sup>41</sup> It was not until the 1978 landmark case *Penn Central Transportation Co. v. City of New York*<sup>42</sup> that the Court handed down a set of factors to consider when determining whether a regulatory taking had, in fact, gone too far.<sup>43</sup> The Court has gone on to hold that the Takings Clause’s requirement for just compensation further extends to construction moratoria,<sup>44</sup> building restrictions devaluing property,<sup>45</sup> inter-

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38. See *United States v. Welch*, 217 U.S. 333, 339 (1910) (holding that the government was required to pay compensation when its taking of a strip of land resulted in destruction of a right of way easement on the adjacent land).

39. See *Miller v. Schoene*, 276 U.S. 272, 280 (1928) (holding that the government ordered destruction of diseased trees did not violate the state police power, thus no due process violation had occurred).

40. 260 U.S. 393 (1922).

41. See *id.* at 415 (holding that state police power allows for the regulation of property to some extent but if it goes too far, it will be recognized as a taking). The opinion recognizes that the government needs some room in which to operate without being made to pay compensation for all incidental effects on property value stemming from its action. *Id.* at 413. While the line may be hard to draw between situations where the government is and is not required to pay compensation, a “strong public desire to improve the public condition is not enough to warrant achieving the desire by a shorter cut than the constitutional way of paying for the change.” *Id.* at 416.

42. 438 U.S. 104 (1978).

43. See *id.* at 124 (“[T]he Court’s decisions have identified several factors that have particular significance. The economic impact of the regulation on the claimant and, particularly, the extent to which the regulation has interfered with distinct investment-backed expectations are, of course, relevant considerations. So, too, is the character of the governmental action. A ‘taking’ may more readily be found when the interference with property can be characterized as a physical invasion by government than when interference arises from some public program adjusting the benefits and burdens of economic life to promote the common good.” (citations omitted)).

44. See, e.g., *First Eng. Evangelical Lutheran Church v. Cnty. of L.A.*, 482 U.S. 304, 322 (1987) (holding that the Fifth Amendment required compensation even for temporary restrictions on land use subsequently invalidated by the court).

45. See, e.g., *Lucas v. S.C. Coastal Council*, 505 U.S. 1003, 1030 (1992) (requiring compensation for regulation that deprives a landowner of all viable economic use of regulated land).

est accruing on money held by a court,<sup>46</sup> and trade secrets.<sup>47</sup> Furthermore, there is ongoing debate as to whether other forms of intangible property—like patents and copyrights, or even cryptocurrency—fall under the protection of the Takings Clause.<sup>48</sup>

### B. *Takings Clause Interactions with Bankruptcy Laws*

As the Takings Clause has evolved and its protections thrown into sharper relief, its application to bankruptcy laws has similarly evolved. In 1935, *Louisville Joint Stock Land Bank v. Radford*<sup>49</sup> dealt with legislation that sought to deprive mortgage-holders of certain property rights during bankruptcy proceedings.<sup>50</sup> Intending to protect farm owners impacted by the dust bowl, the law would have deprived a mortgagee of lien rights to property that it would have retained under state law.<sup>51</sup> The bank, which would have otherwise foreclosed on the property, was prevented from doing so and instead forced to accept court determined rental payments and

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46. See, e.g., *Webb's Fabulous Pharmacies, Inc. v. Beckwith*, 449 U.S. 155, 164 (1980) (holding that the Fifth Amendment forbade Florida courts from retaining interest on funds deposited with the court). The Court explained that “[t]he earnings of a fund are incidents of ownership of the fund itself and are property just as the fund itself is property.” *Id.* “To put it another way: a State, by *ipse dixit*, may not transform private property into public property without compensation, even for the limited duration of the deposit in court. This is the very kind of thing that the Taking Clause of the Fifth Amendment was meant to prevent.” *Id.*

47. See, e.g., *Ruckelshaus v. Monsanto Co.*, 467 U.S. 986, 1016 (1984) (holding that trade secrets are property for the purpose of Fifth Amendment protection).

48. See Jesse Wynn, Note, *Patents, Public Franchises, and Constitutional Property Interests*, 71 CASE W. RES. L. REV. 887, 910–13 (2020) (discussing the long-standing notion that intellectual property is covered by the Takings Clause even though the Supreme Court has never expressly spoken on the issue); Zachary Segal, Note, *Taking Back Bitcoin*, 34 TOURO L. REV. 1375, 1377 (2018) (arguing that Bitcoin is property for Takings Clause purposes under the *Penn Central* test). Segal also suggests that cryptocurrency regulations could potentially be challenged under the Takings Clause. *Id.* at 1379.

49. 295 U.S. 555 (1935).

50. See *id.* at 575–76 (discussing the contours of the Frazier–Lemke Farm Bankruptcy Act). This legislation sought to give bankrupt farmers alternatives to being foreclosed upon. *Id.* at 575. If a farmer was bankrupt and the mortgagee refused to accept a structured statutory payment plan, the bankruptcy court was to “stay all proceedings for a period of five years,” along with other conditions, effectively denying the bank the ability to foreclose on the property. *Id.* at 575–76. The Court held that the Act “has taken from the Bank without compensation, and given to Radford, rights in specific property which are of substantial value.” *Id.* at 601; see also *In re Teleservices Grp.*, 456 B.R. 318, 337 n.61 (Bankr. W.D. Mich. 2011) (noting that while *Radford* itself has since been superseded by statute, the later cases still cite back to *Radford* for the proposition that the bankruptcy power is subject to the limitations of the Fifth Amendment).

51. See *Radford*, 295 U.S. at 579 (discussing the history of bankruptcy protections for debtors, but noting that until the case at issue, no statute or court decision compelled a mortgagee to turn over property free of lien until the debt was paid).

stayed from taking legal action for five years.<sup>52</sup> The Court found that this law violated the Fifth Amendment and announced the oft-repeated phrase: “The bankruptcy power, like the other great substantive powers of Congress, is subject to the Fifth Amendment.”<sup>53</sup>

Two years later, the Court heard *Kuehner v. Irving Trust Co.*,<sup>54</sup> where a bankruptcy provision capped the amount a landlord could claim against a debtor–tenant for terminating a lease.<sup>55</sup> Again, the Court reiterated that “[t]he exercise of the power [to create a provision] is, nevertheless, subject to the commands of the Fifth Amendment.”<sup>56</sup> However, the Court affirmed the constitutionality of the provision, finding that it provided an adequate remedy, and that contract rights, not property rights, were at issue in the case.<sup>57</sup> Thus, the precedent going forward was clear: Congress would be limited by the Fifth Amendment when designing bankruptcy provisions, particularly those that sought to deprive creditors of compensation for property-related rights.<sup>58</sup>

### C. Knick: *Takings Clause Violations and Section 1983*

Adjacent to the dispute over Takings Clause claims in bankruptcy is the related issue of claims for compensation stemming from constitutional violations.<sup>59</sup> Under 42 U.S.C. § 1983, those who have been deprived of constitutional rights by a person acting under the authority of state law

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52. *See id.* at 575–76 (discussing the contours of the Frazier–Lemke Farm Bankruptcy Act and its effect on debtor–creditor lien relations). Ultimately, the Court invalidated the law, stating “the Fifth Amendment commands that, however great the Nation’s need, private property shall not be thus taken even for a wholly public use without just compensation.” *Id.* at 601.

53. *Id.* at 589.

54. 299 U.S. 445 (1937).

55. *See id.* at 447 (analyzing a bankruptcy statute that limited the “claim of a landlord for indemnity under a covenant in a lease to an amount not to exceed three years’ rent”). The creditor had leased real estate to a cigar store that went bankrupt. *Id.* The creditor wanted to bring a claim for lost rent in excess of the statutory three-year limit. *Id.* at 448.

56. *Id.* at 451.

57. *See id.* at 453–54 (holding that the provision did provide landlords a reasonable and certain remedy for their damages, and that the provision was not arbitrary or discriminatory, which would cause it to run afoul of the Fifth Amendment).

58. *See United States v. Sec. Indus. Bank*, 459 U.S. 70, 75–78, 81–82 (1982) (citing *Radford* to establish that the bankruptcy Code is subject to the Fifth Amendment). The Court refused to retroactively apply a bankruptcy statute that would have destroyed lien rights against debtor’s property. *Id.* at 80–81. While the case turned on principles of retroactivity, the court “decline[d] to construe the Act in a manner that could in turn call upon the Court to resolve difficult and sensitive questions arising out of the guarantees of the [Takings Clause].” *Id.* at 82 (quoting *NLRB v. Catholic Bishop of Chi.*, 440 U.S. 490, 507 (1979)).

59. For a discussion of both types of claims that arose in the Detroit bankruptcy that raised constitutional concerns, see *supra* notes 13–15 and accompanying text.

may seek a statutory remedy.<sup>60</sup> Section 1983 provides remedies for a broad range of civil rights violations that could be perpetrated by various types of state actors.<sup>61</sup> For example, in *In re Detroit*, the court lumped together the § 1983 Creditors in addressing the dischargeability of such claims.<sup>62</sup> Those claimants had all filed lawsuits against the city for actions taken by city officials, alleging “various violations of their constitutional rights, including those guaranteed by the First, Fourth, Fifth, Sixth, Seventh, and Fourteenth Amendments.”<sup>63</sup>

Protection from governmental takings, however, is structured differently than the other constitutional rights. The Fifth Amendment does not forbid the taking of private property, rather, it requires just compensation for the government’s taking of private property; the government’s failure to pay just compensation transforms the act into a violation of the Amendment.<sup>64</sup> States have thus created laws to provide for compensation when a

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60. See 42 U.S.C. § 1983 (1996) (providing that “[e]very person who, under color of any statute, ordinance, regulation, custom, or usage, of any State or Territory or the District of Columbia, subjects, or causes to be subjected, any citizen of the United States or other person within the jurisdiction thereof to the deprivation of any rights, privileges, or immunities secured by the Constitution and laws, shall be liable to the party injured in an action at law, suit in equity, or other proper proceeding for redress”).

61. See generally ANNE H. TURNER, SECTION 1983: OVERVIEW (2023), Westlaw W-001-8382 (overviewing the contours and requirements of Section 1983). Claims under this Section may be brought by individual citizens, aliens, or corporations. *Id.* The term “person” as used in the statute to denote the entity committing the violation has been interpreted to include local government employees, local government entities, State or United States Territory employees acting in their individual capacity, and private individuals acting for state or local government. *Id.* Regarding the rights protected, “Plaintiffs may enforce a wide variety of constitutional rights using Section 1983” including claims for violations of procedural and substantive due process, equal protection under the law, and rights incorporated from the Bill of Rights. *Id.* Turner identifies several incorporated rights enforceable under § 1983: First Amendment freedoms of speech, press, assembly, petition, and religions; Second Amendment right to keep and bear arms; Fourth Amendment protection against unreasonable searches and seizures; Fifth Amendment protection from self-incrimination and the right to just compensation for the taking of private property; Sixth Amendment right to confront witnesses, trial by jury, and counsel; and the Eighth Amendment protections against excessive bail and cruel and unusual punishment. See also *McDonald v. City of Chi.*, 561 U.S. 742, 764 n.12 (2010) (tracing the incorporation of a majority of the rights secured by the Bill of Rights; violations of which may form the bases for § 1983 claims against a state body or actor).

62. *In re City of Detroit*, 524 B.R. 147, 262 (Bankr. E.D. Mich. 2014) (analyzing the claims of “two distinct groups” of “unsecured creditors that have constitutional claims against the City or its officers”). The first group was seeking to recover “damages for the deprivation of their constitutional rights under 42 U.S.C. § 1983.” *Id.* The second group had “lawsuits to recover on their just compensation claims under the Fifth Amendment for the City’s alleged taking of their property.” *Id.*

63. *Id.* at 263.

64. See U.S. CONST. amend. V (“[N]or shall private property be taken for public use, without just compensation.”).

taking occurs and legal recourse for victims of takings who believe they have been shortchanged.<sup>65</sup> This duality of protections at the state and federal level, presents a quandary for uncompensated takings victims: whether to first pursue state remedies for compensation or to turn immediately to federal relief for a constitutional violation.<sup>66</sup> Prior to 2019, Supreme Court precedent held that individuals were not permitted to bring a Takings Clause violation claim in federal court until a state court had fully adjudicated the matter and denied compensation.<sup>67</sup>

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65. *See, e.g., In re City of Stockton*, 909 F.3d 1256, 1260–61 (9th Cir. 2018) (describing the California procedure for direct takings). In this case, the Stockton City Council decided to use the power of eminent domain to condemn a strip of land to build a road. *Id.* at 1260. California law provided for a direct “condemnation proceeding” where the state could initiate the action in court and pay compensation at judgment when the government takes control of the land, or the “quick-take” provision whereby state or local government could take possession of private property by appraising the property and depositing a probable amount of compensation with the state Condemnation Deposit Fund. *Id.* at 1260–61. However, even when the quick-take procedures are used and the former property owner withdraws the funds, they may still bring a “claim for greater compensation.” *Id.* at 1261; *see also* *Knick v. Twp. of Scott*, 139 S. Ct. 2162, 2168 (2019) (discussing state inverse condemnation statutes). “Inverse condemnation stands in contrast to direct condemnation, in which the government initiates proceedings to acquire title under its eminent domain authority.” *Id.* Inverse condemnation is a cause of action brought by a property owner to “recover the value of property” that has been taken by the government. *Id.* For example, in this case, local government had placed a requirement on property owners to keep cemeteries “open and accessible to the general public during daylight hours,” a regulation that potentially devalued the property. *Id.* While the property owner here did not bring a state inverse condemnation action, the court noted that “Pennsylvania, like every other State besides Ohio, provides a state inverse condemnation action.” *Id.*

66. *See Knick*, 139 S. Ct. at 2167 (recounting the difficulties surrounding availability and timing of federal and state claims for just compensation). Prior to *Knick*, takings plaintiffs were required to go to state court before bringing their claim in federal court. *Id.* However, the Supreme Court also held that state court resolutions of just compensation claims had a preclusive effect on later federal suits. *Id.* The Court described this conundrum as “a Catch-22: He cannot go to federal court without going to state court first; but if he goes to state court and loses, his claim will be barred in federal court.” *Id.*

67. *See Williamson Cnty. Reg’l Plan. Comm’n v. Hamilton Bank of Johnson City*, 473 U.S. 172, 200 (1985) (holding that a § 1983 claim for an uncompensated taking was premature because plaintiff had not applied for variances from the state regulations, and findings were incomplete as to the property value and effect on investment backed expectations).

In *Knick v. Township of Scott*,<sup>68</sup> the Supreme Court reversed this earlier precedent.<sup>69</sup> In *Knick*, petitioner owned a large tract of land where a township officer discovered an old cemetery on the property.<sup>70</sup> Petitioner was notified that she had violated a township ordinance that required all cemeteries to be kept open to the public during the day.<sup>71</sup> Petitioner filed suit for declaratory and injunctive relief on the basis that the ordinance was a taking of her property.<sup>72</sup> The petitioner's suit motivated the township to stay enforcement and, without any ongoing harm to point to, the state court refused to rule on the declaratory and injunctive relief.<sup>73</sup> Petitioner then filed in federal court under § 1983, alleging that the local ordinance violated the Takings Clause; however, the case was dismissed in district court.<sup>74</sup> Vacating the lower court's decision and overruling past precedent, the Supreme Court held that "[a] property owner may bring a takings claim under § 1983 upon the taking of his property without just compensation by a local government."<sup>75</sup>

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68. 139 S. Ct. 1262 (2019).

69. *See id.* at 2167 (acknowledging that the earlier decision to require state court denial of just compensation under state law before allowing a federal takings claim was based on "a mistaken view of the Fifth Amendment"). Overturning past precedent, the *Knick* court held that "the property owner has suffered a violation of his Fifth Amendment rights when the government takes his property without just compensation, and therefore may bring his claim in federal court under § 1983 at that time." *Id.*

70. *See id.* at 2168 (detailing that the *Knick*'s property contained a small graveyard allegedly containing ancestors of the *Knick*'s neighbors and explaining that small family graveyards like these are common in Pennsylvania).

71. *See id.* (noting that the Township of Scott had passed an ordinance in 2012 requiring all cemeteries remain open to the public during the day). The definition of "cemetery" was quite broad: "[a] place or area of ground, whether contained on private or public property, which has been set apart for or otherwise utilized as a burial place for deceased human beings." *Id.* (alteration in original).

72. *See id.* (discussing the suit brought by petitioner in state court). Notably, *Knick* did not seek compensation through an inverse condemnation suit. *Id.* Rather, *Knick* styled her complaint as one for both declaratory and injunctive relief on the theory that the government regulation violated the Fifth Amendment. *Id.*; *see also supra* note 65 (discussing the differences between inverse condemnation and direct condemnation).

73. *See id.* ("In response to *Knick*'s suit, the Township withdrew the violation notice and agreed to stay enforcement of the ordinance during the state court proceedings. The court, however, declined to rule on *Knick*'s request for declaratory and injunctive relief because, without an ongoing enforcement action, she could not demonstrate the irreparable harm necessary for equitable relief.").

74. *See id.* at 2169 (discussing the district court's decision to dismiss the case). Prior to this case, past precedent had required the takings victim to exhaust her inverse condemnation action in state court before coming to federal court. *Id.* The district court dismissed her case because she had failed to pursue an inverse condemnation action in state court, opting only to seek declaratory and injunctive relief. *Id.*

75. *Id.* at 2179 (clarifying that the suits for uncompensated takings can be brought in federal court at the time the property is taken without having to wait for state court proceeding to deny compensation).

D. *Collision of Case Lines*

While consumer bankruptcy filings and corporate restructurings are mine-run bankruptcy occurrences, large municipal Chapter 9 filings are far less common.<sup>76</sup> Therefore, allegations of Takings Clause violations have historically targeted the *operation* of a bankruptcy statute—specifically, where a creditor is deprived of property rights through the bankruptcy process—not the direct action of the debtor.<sup>77</sup> Municipal bankruptcies present the far less common situation where a government entity has taken an eminent domain action—or is liable for an inverse condemnation claim—before entering bankruptcy, and then seeks to have that debt discharged.<sup>78</sup>

The Michigan Eastern District Bankruptcy Court addressed the potential discharge of debts for takings as an issue of first impression in *In re Detroit*.<sup>79</sup> The court started its analysis with the time-worn maxim of *Radford*, stating that “bankruptcy proceedings are subject to the Fifth Amendment’s prohibition on public takings of private property without just compensation.”<sup>80</sup> However, it ultimately relied on the United States Attorney General’s recommendation that the court simply use discretionary powers to exempt the claim from discharge and avoid the constitutional question.<sup>81</sup> In the same breath, however, the court held that discharging § 1983 claims against the city did not violate the Constitution.<sup>82</sup>

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76. See David Skeel, *Reflections on Two Years of P.R.O.M.E.S.A.*, 87 REV. JUR. U. P.R. 862, 864 (2018) (describing the use of municipal bankruptcies to restructure large city debt as a recent development).

77. For a discussion of the various types of bankruptcy statutes that were struck down as unconstitutional attempts on Congress’s part to deprive creditors of property rights through the bankruptcy process, see *supra* Section II.B.

78. See *In re City of Detroit*, 524 B.R. 147, 267 (Bankr. E.D. Mich. 2014) (describing the Takings Clause creditors with claims against the city). One creditor had a “prospective monthly just compensation damage award” for ongoing land use restrictions. *Id.* Two other creditors had pending suits against the city for just compensation. *Id.* These creditors argued that the city’s plan was unconstitutional because it “treats their claims as general unsecured claims and impairs them”).

79. See *In re Detroit*, 524 B.R. at 268 (“[T]he specific issue of whether a municipal debtor in a [C]hapter 9 bankruptcy case may impair a creditor’s claim for just compensation under the Fifth Amendment is one of first impression.”).

80. *Id.* at 269.

81. See *id.* at 262 (agreeing with the assessment of the Attorney General). The Court had permitted the Attorney General of the United States to intervene specifically on the constitutional questions regarding Chapter 9. *Id.* Specifically, the Attorney General asserted that impairing Takings Clause claims would “raise substantial constitutional concerns” and recommended that the court “avoid that issue” by using its equitable powers to except those claims from discharge. *Id.*

82. See *id.* at 263 (relying on the suggestion of the Attorney General that discharge of § 1983 claims does not present a constitutional issue); see also Jacoby, *supra* note 3, at 59 n.22 (explaining that the Detroit bankruptcy created new precedent because it allowed for impairment of pensions, and created new law by allowing the discharge of civil rights claims but preventing the impairment of Takings Clause claims); *In re Nifong*, No. 08-80034C-7D, 2008 WL 2203149 (Bankr.



The same issue surfaced in the Stockton bankruptcy four years later when the Ninth Circuit heard *In re City of Stockton*.<sup>83</sup> Andrew Cobb owned a parcel of land in Stockton that the city condemned in 1998.<sup>84</sup> California law mandated that as part of a condemnation action, the city was required to set aside funds for probable compensation.<sup>85</sup> Former property owners could then withdraw the funds on the condition that they waive all claims and defenses to the condemnation, except for a claim for greater compensation.<sup>86</sup> Cobb passed away and his son withdrew the funds, only to subsequently attempt to return them and pursue an action for greater compensation.<sup>87</sup> In 2011, Cobb's claim reached the Court of Appeals, where he was set to proceed with his inverse condemnation suit, only to be stymied by Stockton's 2012 Chapter 9 filing.<sup>88</sup>

Cobb filed a proof of claim but did not object to being listed as an unsecured creditor.<sup>89</sup> Cobb then objected to the city's plan, arguing that the Takings Clause protected his claim from impairment.<sup>90</sup> The Ninth Circuit ultimately held against him, finding that he had waived any property interest by withdrawing the funds fifteen years earlier, and that his claim for just compensation was simply "an unsecured monetary debt claim."<sup>91</sup> Notably, the court seemed to pull back from the *Radford* mantra,

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M.D.N.C. May 27, 2008) (finding that in Chapter 7 bankruptcy of an individual debtor, § 1983 claims were not entitled to any immunity from discharge).

83. 909 F.3d 1256 (9th Cir. 2018).

84. *See id.* at 1260 (describing the facts surrounding the condemnation). Andrew Cobb, the father of the plaintiff in the 2018 case, owned a parcel of land in Stockton. *Id.* The Stockton City Council resolved to condemn a strip of land cutting across the parcel to construct a road. *Id.*

85. *See id.* at 1261 (describing the California "quick-take" condemnation procedure (quoting Cal. Civ. Proc. Code § 1255.410 (West 2023))). Localities were permitted to exercise eminent domain and take immediate possession of a property by "depositing a probable compensation amount determined by a qualified expert appraiser." *Id.*

86. *See id.* (noting that the effect of a Takings Clause violation victim's election to withdraw from the set aside amount will waive all claims and defenses except for a claim of greater compensation).

87. *See id.* (explaining that Andrew Cobb passed away before condemnation proceedings were completed, so his son inherited the parcel and took over the condemnation action). Subsequently, the son withdrew the entire amount without asserting a counterclaim for greater compensation. *Id.*

88. *See id.* at 1262 (relating the city's decision to list Cobb as an unsecured, disputed liability claim in the Chapter 9 filing). Cobb then filed his "proof of claim for \$4,200,997.26. Cobb's claim consisted of a principal of \$1,540,000.00 for the parcel, \$2,282,997.26 in interest on the principal, \$350,000.00 in attorney's fees and expenses, \$13,000.00 in costs of suit, and \$15,000.00 in real estate taxes and maintenance and insurance costs." *Id.*

89. *See id.*

90. *See id.* at 1266 ("Cobb filed an objection to confirmation of the plan, alleging that his 'claims in inverse condemnation are protected by the Fifth and Fourteenth Amendments to the United States Constitution and cannot be impaired by the Plan.' He did not contest the listing of his claim as unsecured.").

91. *See id.* at 1267, 1269 (resting its decision on equitable mootness grounds due to Cobb's failure to raise issues in a timely manner, and that the bankruptcy

suggesting that “in a number of contexts the Code expressly permits the adjustment of debts of secured creditors, including lien rights.”<sup>92</sup> Judge Friedland’s dissent, however, advocated for the absolutism of the *Radford* mantra, insisting that the Takings Clause prohibits any impairment of “substantive rights in specific property.”<sup>93</sup> Judge Friedland felt that Cobb had taken all necessary steps to preserve his claim, and that the potential claim for “greater compensation” was guaranteed by the Fifth Amendment.<sup>94</sup>

*In re Detroit* and *In re Stockton* were handed down in 2014 and 2018, respectively.<sup>95</sup> In both cases, Takings Clause claimants against the bankrupt city would not have had valid § 1983 claims until the states’ respective processes denied them just compensation.<sup>96</sup> However, post-*Knick*, which was decided in 2019, the constitutional violation occurs *at the time of the taking* and a prima facie § 1983 claim exists at that moment.<sup>97</sup> Though this new distinction seems formalistic, it may be incredibly important whether a creditor is alleging a pre-petition debt for a takings claim under § 1983 or arguing that the discharge of a pending state takings claim through bankruptcy violates the Fifth Amendment.<sup>98</sup>

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had already been significantly consummated). Again, the court declined to take the constitutional issue head on, relying instead on these alternative grounds but suggesting that the Takings Clause would not bar discharge of Cobb’s claim. *Id.* at 1267.

92. *Id.* at 1268 (quoting SOMMER & LEVIN, *supra* note 7, ¶ 506.02).

93. *Id.* at 1272 (Friedland, J., dissenting) (quoting *Louisville Joint Stock Land Bank v. Radford*, 295 U.S. 555, 590 (1935)).

94. *See id.* at 1278–80 (suggesting that the guarantee of just compensation is limited to Takings Clause violations and repeating the rationale of the *In re Detroit* court that vindication of other constitutional rights through compensatory damages, like § 1983 claims, may continue to be impaired in bankruptcy).

95. *See generally In re City of Detroit*, 524 B.R. 147, 268 (Bankr. E.D. Mich. 2014); *In re Stockton*, 909 F.3d at 1256 (deciding the issue in 2018).

96. *See Knick v. Twp. of Scott*, 139 S. Ct. 1262 (2019) (acknowledging that prior to the *Knick* decision in 2019, the now-overturned precedent was that “a property owner whose property has been taken by a local government has not suffered a violation of his Fifth Amendment right—and thus cannot bring a federal takings claim in federal court—until a state court has denied his claim for just compensation under state law”).

97. For a discussion of the holding in *Knick* and current Supreme Court precedent on the timing of federal Takings Clause violation claims, see *supra* notes 64–71 and accompanying text.

98. *See* SOMMER & LEVIN, *supra* note 7, ¶ 502.03[1][b] (describing the significance of the bankruptcy petition date on claims). Section 502(b) of the Code “requires that a claim be determined ‘as of the date of the filing of the petition.’” *Id.* Creditor must submit a “proof of claim” that can only contain “claims as of the petition date or those claims deemed to arise as of or before the petition date.” *Id.*; *In re Detroit*, 524 B.R. at 265 (holding that the Detroit plan did not violate the Fourteenth Amendment by discharging § 1983 claims). The creditors argued that their right to statutory remedies through § 1983 was constitutionally protected and that to impair those claims was a violation of law, but the court found neither argument persuasive. *Id.* at 263–65; *In re Stockton*, 909 F.3d at 1266 (“If the purported property interest is, in reality, just a contractual or statutory right for mone-

### III. PROMESA'S SHIP-OF-THE-LINE: THE FACTS OF THE PUERTO RICAN BANKRUPTCY

The central case of this Note originated in Puerto Rico's 2017 bankruptcy.<sup>99</sup> In 2015, when Puerto Rico failed to fulfill its debt obligation, Congress responded by passing the Puerto Rico Oversight, Management, and Economic Sustainability Act (PROMESA).<sup>100</sup> While in a typical municipal bankruptcy, filed under Chapter 9, the city or municipality remains in control, in this case PROMESA created an Oversight Board with the power to "certify fiscal plans for Puerto Rico . . . and restructure Puerto Rico's debts."<sup>101</sup> While PROMESA functions separately from a traditional Chapter 9 bankruptcy, Congress's "eyes were on Chapter 9" in the creation of PROMESA, and Chapter 9 precedent figures heavily into the First Circuit's eventual resolution of the Takings Clause issues.<sup>102</sup>

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tary relief, then the debt can be adjusted in bankruptcy."). The court characterized the claim as an "unsecured monetary claim" and pointed out that "when Stockton filed its bankruptcy petition, Cobb did not possess a property interest cognizable as such in bankruptcy, and he never asserted anything but an unsecured proof of claim." *Id.* at 1266–68.

99. *See generally* Skeel, *supra* note 76, at 862 (discussing the circumstances in which Puerto Rico filed for Chapter 9 bankruptcy and Congress's passage of PROMESA). While Puerto Rico had a "vibrant economy" in the 1950s and 1960s, it "experienced financial distress for over a decade" until in 2015, the governor "declared the island unable to pay its debts." *Id.*; Michael Corker, *Puerto Rico Faces Its Creditors in Early Debt Resolution Talks*, N.Y. TIMES (July 13, 2015), <https://www.nytimes.com/2015/07/14/business/puerto-rico-faces-its-creditors-in-early-debt-resolution-talks.html> [<https://perma.cc/YMX7-E3VF>] (reporting on an early meeting between Puerto Rico and its creditors, and opining that "restructuring the island's \$72 billion in debt could be a long process"). The article discusses how some investors were frustrated "that Puerto Rico officials [were] painting an overly dark picture to drum up support in Congress for some form of federal assistance." *Id.*

100. *See* Skeel, *supra* note 72, at 862; *see also* Corker, *supra* note 99 (explaining that Puerto Rico was lobbying Congress for aid in 2015 because "as a United States territory" they did not have access to the federal bankruptcy courts).

101. *See* Skeel, *supra* note 72, at 870.

102. *See id.* at 873 (discussing the creation of Title III of PROMESA and the similarities between it and Chapter 9). Skeel explains that PROMESA provided similar protections to Chapter 9 in that it provides "only for voluntary filings" and "an automatic stay prohibiting creditors from continuing to pursue non-bankruptcy collection efforts goes into effect as soon as the debtor files." *Id.* A notable difference, however, is that PROMESA allowed Puerto Rico itself to be a bankrupt entity as opposed to Chapter 9, "which applies to municipal entities within a state but not to the state." *Id.*; *In re Fin. Oversight & Mgmt. Bd.*, 41 F.4th 29, 44–45 (1st Cir. 2022) (looking to the decisions in the Detroit and Stockton Chapter 9 bankruptcies in its analysis of whether a just compensation claim is different than other kinds of constitutional violations), *cert. denied* 143 S. Ct. 774 (2023). The First Circuit explicitly praises the reasoning in Judge Friedland's dissent in the Ninth Circuit opinion and cites *In re Detroit* for confirmation of their view that "the Fifth Amendment prohibits the discharge or impairment of claims for just compensation in bankruptcy." *Id.* at 45.

The Oversight Board was tasked with finding a way to return Puerto Rico to a state of fiscal responsibility, which would take years of effort.<sup>103</sup> The board faced a variety of obstacles, including two major hurricanes that ravaged the Commonwealth just a year after the passage of PROMESA and the COVID-19 pandemic.<sup>104</sup> However, in January 2022, the Oversight Board proposed its modified eighth amended plan, and the court confirmed it over all objections, save for one class: “Eminent Domain/Inverse Condemnation Claims.”<sup>105</sup>

Several creditors had filed claims seeking compensation for uncompensated takings that had occurred prior to the bankruptcy filing.<sup>106</sup> Similar to the circumstances in Stockton, Puerto Rico utilized a “quick take”

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103. See Skeel, *supra* note 72, at 871 (relating the purpose of PROMESA and the requirements placed on the Oversight Board by Congress). The Board was empowered to “certify fiscal plans for Puerto Rico and any ‘covered’ municipal entities.” *Id.* Skeel notes:

Under P.R.O.M.E.S.A., each fiscal plan must cover at least the next five years. It also must seek to “restore fiscal responsibility and access to the capital markets,” and satisfy a list of fourteen different requirements, from “provid[ing] for estimates of revenues and expenditures” to “respect[ing] the relative lawful priorities or lawful liens.”

*Id.* (alterations in original) (quoting Puerto Rico Oversight, Management, and Economic Stability Act, 48 U.S.C. § 2141(a) (2018)).

104. See RAND CORP., *Hurricanes Irma and Maria: Impact and Aftermath*, <https://www.rand.org/hsrd/hsoac/projects/puerto-rico-recovery/hurricanes-irma-and-maria.html> [<https://perma.cc/9P63-5UZ5>] (last visited May 15, 2023) (reporting on Hurricanes Irma and Maria—category 4 and 5 storms, respectively—which hit Puerto Rico in September 2017, rendering all seventy-eight of Puerto Rico’s municipalities eligible for FEMA assistance); Skeel, *supra* note 72, at 877 (describing testimony of Hurricane Maria). “It sounded like an airplane roaring to life, over and over, for twelve hours.” *Id.* “[T]he hurricanes may have caused more than 4000 deaths, many because access to medical treatment was cut off.” *Id.*

105. See *In re Fin. Oversight & Mgmt. Bd.*, 636 B.R. 1, 6 (D.P.R. 2022) (confirming the plan and holding that any objections in opposition or inconsistent with the plan were overruled and denied, except for a “narrow exception of the objections of holders of alleged Eminent Domain/Inverse Condemnation Claims, which are hereby SUSTAINED to the extent that such Claims are ultimately Allowed Claims”); see also *In re Fin. Oversight & Mgmt. Bd.*, 637 B.R. 233, 239–41 (D.P.R. 2022) (discussing at length the facts found by the district court and elucidating the narrow class of Takings Clause claimants that were exempt from discharge). Notably, the court dismissed contentions by a class of bondholders who raised Takings Clause arguments by finding that their circumstances did not amount to a regulatory taking. *Id.* at 298–99. Similarly, *Suiza Dairy* was denied Fifth Amendment protection for its claim against the Commonwealth, where *Suiza Dairy* had adjudicated a regulatory taking claim against the Commonwealth that ended in settlement. *Id.* at 299–300. Despite Fifth Amendment just compensation being the impetus for such a settlement, the court found that *Suiza Dairy* “merely has a contract-based claim for payment,” which is susceptible to adjustment or discharge in bankruptcy. *Id.*; *Vaqueria Tres Monjitas, Inc. v. Irizarry*, 587 F.3d 464, 468–71 (1st Cir. 2009) (describing the milk regulation enacted in Puerto Rico and *Suiza Dairy*’s constitutional challenge to it, alleging it violated the Takings Clause).

106. See *In re Fin. Oversight & Mgmt. Bd.*, 41 F.4th 29, 38 (1st Cir. 2022) (“In the lead up to the plan’s development, several groups of creditors (the ‘takings claimants’) filed proofs of claim with the Title III court seeking just compensation

statute for acquiring property through eminent domain and several of the creditors had potential claims for greater compensation that had not been taken to judgment.<sup>107</sup> Additionally, other creditors, similar to the property owner in *Knick*, had inverse condemnation claims against the Commonwealth.<sup>108</sup> The district court held that nothing in the plan “shall impair or otherwise affect the treatment” of allowed eminent domain or inverse condemnation claims, and that such claims were entitled to receive full compensation and not be treated as unsecured claims.<sup>109</sup> The board promptly appealed this ruling to the First Circuit.<sup>110</sup>

IV. THE FIRST CIRCUIT’S MAIDEN VOYAGE: A NARRATIVE ANALYSIS OF THE FIRST CIRCUIT’S DECISION TO FIND TAKINGS CLAUSE CLAIMS NONDISCHARGEABLE IN *IN RE FINANCIAL OVERSIGHT*

The overarching issue before the First Circuit in *In re Financial Oversight* was whether the district court erred in holding that eminent domain and inverse condemnation claims were immune from impairment.<sup>111</sup> The parties did not dispute that a governmental taking had occurred and that a reasonable factfinder could determine that just compensation had not been made.<sup>112</sup> Rather, the dispute centered on whether the Fifth Amend-

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for alleged prepetition takings of their private property by the Commonwealth.”), *cert. denied* 143 S. Ct. 774 (2023).

107. *See id.* Describing the operation of the Puerto Rico quick take eminent domain statute, the court noted:

That statute permits the Commonwealth to acquire private property through eminent domain by depositing an estimated compensation amount with the Puerto Rico court of first instance. If the owner of the taken property regards the deposit as insufficient, the owner may seek a court determination of just compensation. Should just compensation exceed the amount of the deposit, the Commonwealth must pay the difference.

*Id.*; *see also supra* notes 85–86 and accompanying text (describing the California quick take procedure).

108. *See In re Fin. Oversight*, 41 F.4th at 38 (describing the inverse condemnation claims as those that “arose out of takings in which the Commonwealth allegedly curtailed an owner’s property right without first tendering a deposit. In such instances, the owner may simply sue the Commonwealth for payment in full of just compensation after the physical taking has occurred”); *see also supra* note 65 (discussing inverse condemnation as described by the Supreme Court in the *Knick* decision).

109. *See In re Fin. Oversight & Mgmt. Bd.*, 636 B.R. at 50–51 (stating that nothing should be construed to prevent a determination of just compensation and potentially allowed for interest on the allowed eminent domain and inverse condemnation claims).

110. *See In re Fin. Oversight*, 41 F.4th at 39 (relating the numerous appeals by creditors to various aspect to the plan, including the Board challenging the ruling of the lower court holding that “the Fifth Amendment precludes the plan from impairing prepetition claims for just compensation that arise under the Takings Clause”).

111. *Id.*

112. *Id.* at 41.

ment prevented impairment of these claims for just compensation.<sup>113</sup> The First Circuit initially considered whether the constitutional question should even be addressed.<sup>114</sup> Satisfied that it was necessary to address the question, the court then considered the two major contentions by the Oversight Board: (1) that in bankruptcy proceedings, the Fifth Amendment only prohibits impairment of rights in property at the time of filing, not unsecured prepetition claims for money, and (2) that a claim for just compensation is no different from other claims for monetary compensation resulting from constitutional violations.<sup>115</sup> The First Circuit also acknowledged three minor points raised by the Oversight Board, all addressed below.<sup>116</sup>

#### A. *Constitutional Avoidance*

The Bankruptcy Code provides the court with a statutory basis for broad equitable powers and discretionary judgment.<sup>117</sup> As intervenor, the United States suggested that the court could simply sidestep the constitutional issue by relying on 11 U.S.C. § 944(c)(1), which allows the court to use its equitable powers to decide that a particular debt is not dischargea-

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113. *Id.* at 39 (clarifying that this opinion only addresses “the Board’s cross-appeal challenging the ruling of the Title III court that the Fifth Amendment precludes the plan from impairing prepetition claims for just compensation”).

114. *See id.* at 39–40 (presenting the rationale for confronting the constitutional question presented). The United States was an intervenor in the case and recommended that the court avoid the constitutional question by using the discretionary equitable powers granted under 11 U.S.C. § 944(c)(1)—the same recommendation it made to the Michigan district court in the Detroit bankruptcy. *Id.* The court declined to use § 944(c)(1) to sidestep the constitutional question in part because the lower court did not invoke it. *Id.* at 40. Additionally, the court recognized that even to use discretionary power to prevent the impairment of the claims, it would still need to provide reasoning for that decision, ultimately needing to address the Fifth Amendment anyway. *Id.* For a discussion of the position taken by the United State as intervenor in the Detroit bankruptcy, see *supra* note 14.

115. *See In re Fin. Oversight*, 41 F.4th at 41–42 (deciding to address each of these two major concerns in turn, undermining the position taken by the Board that obligations to pay just compensation can be impaired in bankruptcy).

116. *See id.* at 45 (describing these last three points as “three other brief rejoinders meriting our attention”). The Board argued that just compensation claims are often modified by law without offending the Fifth Amendment in other contexts, that remedies for Takings Clause violations should not be treated differently than other remedies for constitutional violations, and that preventing impairment of these claims will endanger the viability of future municipal restructurings. *Id.* at 46.

117. *See* 11 U.S.C. § 105(a) (2018) (“The court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title. No provision of this title providing for the raising of an issue by a party in interest shall be construed to preclude the court from, sua sponte, taking any action or making any determination necessary or appropriate to enforce or implement court orders or rules, or to prevent an abuse of process.”).

ble.<sup>118</sup> The court, however, declined to follow this advice due to the reasoning of the district court.<sup>119</sup> The lower court had specifically ruled the Takings Clause claims nondischargeable on constitutional grounds, not on discretionary grounds.<sup>120</sup> Ultimately, the First Circuit found that it was not able to skirt the constitutional thicket; thus, it took the Oversight Board's contentions in turn.<sup>121</sup>

B. *First Argument: The Takings Clause Only Protects Rights to Property at the Time of Petition*

The Oversight Board's first contention with the district court's holding was that the Takings Clause protection only applied to the specific rights in private property held at the time of the debtor's filing.<sup>122</sup> Because the takings occurred before the bankruptcy, the Board argued that "any constitutional violation would have arisen only at the time of the taking" and because the creditors no longer possess property rights, "the takings claimants now merely possess unsecured claims for money, which may be adjusted in bankruptcy without issue."<sup>123</sup> Citing to *Knick* for support, the Board argued that because the claim for a Takings Clause violation

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118. See *In re Fin. Oversight*, 41 F.4th at 39–40 (relating the suggestions of the AG); see also *supra* note 114 (describing the AG's proposed resolution utilizing § 944(c)(1) and the court decision not to accept the proposal).

119. See *id.* at 40–41.

120. Compare *id.* at 41 (claiming the Detroit bankruptcy was the only time section 944(c)(1) was invoked for constitutional grounds and affirming that the *In re Detroit* court held that "discharging prepetition claims for just compensation in bankruptcy would violate the Fifth Amendment"), with *In re City of Detroit*, 524 B.R. 147, 262 (Bankr. E.D. Mich. 2014) ("The Attorney General does assert, however, that impairing claims under the Takings Clause of the Fifth Amendment would raise substantial constitutional concerns. The Attorney General suggested that to avoid that issue, if the plan is confirmed, the confirmation order should explicitly except the Takings Clause claims from discharge, as § 944(c)(1) permits in the Court's discretion. The Court agreed with the Attorney General's analysis." (emphasis added)).

121. See *In re Fin. Oversight*, 41 F.4th at 41 ("Thus, while we appreciate the wisdom of declining to venture into a constitutional thicket when the resolution of an independent issue would present a clearer path, we see no such opportunity to do so here."). The court rejected the advice of the United States to dispose of the issue on equitable grounds and avoid the constitutional issue; instead, it cited the *In re Detroit* court as having "effectively answered the constitutional question the United States would have us avoid here." *Id.* However, the Detroit court was in precisely the same position and appears to have taken the advice of the U.S. Attorney General in avoiding the constitutional question while simultaneously assuming the Fifth Amendment would have barred the discharge of Takings Clause claims regardless. See *In re Detroit*, 524 B.R. at 262, 268.

122. See *In re Fin. Oversight*, 41 F.4th at 42 (discussing the board's argument that because, post-*Knick*, the constitutional violation arises at the time of the taking, "just compensation as an entitlement to payment[ ] is untethered from the substantive Takings Clause violation itself").

123. *Id.* at 42–43.

vests as soon as the taking occurs, it was alike in kind to other prepetition claims for monetary compensation stemming from constitutional violations.<sup>124</sup>

The court was unpersuaded, finding that *Knick* should not be read to allow the conversion of Takings Clause violations into monetary obligations that could then be statutorily disposed of.<sup>125</sup> The court also dismissed as “inapposite” several lower court cases that distinguished between specific property rights and money claims where impairment is permitted.<sup>126</sup> Accordingly, the court drew a line between cases where the issue was *whether* a taking had occurred and the present issue regarding impairment of an acknowledged just compensation claim, stating “[u]nless a provision prevented the full payment of a claim for just compensation, it would not implicate the issue we decide here.”<sup>127</sup>

C. *Second Argument: Takings Clause Violations are No Different from Other Constitutional Violations*

Secondly, the Oversight Board suggested that a claim for just compensation should be treated the same as other claims for compensation for constitutional violations, and consequently adjustable as claims for money damages.<sup>128</sup> The First Circuit, however, took the language of the Takings Clause to be a textual cue that just compensation is different in kind from § 1983 claims.<sup>129</sup> The court found it significant that the Constitution itself provided the remedy, noting, “in the case of the Takings Clause, the Constitution clearly spells out both a monetary remedy and even the necessary quantum of compensation due.”<sup>130</sup> The First Circuit found Judge Friedland’s dissent in *In re Stockton* to be compelling and reasoned that Takings

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124. *See id.* (describing the Board’s reliance on *Knick* and its rejection of previous precedent on the timing of a vested takings claim); *see also* *Knick v. Twp. of Scott*, 139 S. Ct. 2162, 2170 (2019) (holding that victims of uncompensated takings were not required to pursue state law claims for just compensation before proceeding in federal court under a § 1983 claim). *Knick* notably overturned precedent that had required just the opposite and had been the standing precedent during the *In re Detroit* and *In re Stockton* filings. *Id.*

125. *See In re Fin. Oversight*, 41 F.4th at 43.

126. *See id.* (distinguishing the Supreme Court decision in *Kuehner* as being directed at determining whether a taking of property had occurred at all, not the issue on appeal here). The First Circuit recognized that to assume that just compensation claims are simply contractual claims for money, it “begs the very question raised by this appeal.” *Id.* For a discussion of the facts and circumstance of the *Kuehner* case, *see supra* note 55.

127. *Id.* at 44.

128. *See id.* at 44 n.6 (assuming without deciding that claims for monetary compensation for other constitutional violations can be impaired or discharged).

129. *See id.* at 45–46 (distinguishing takings claims as those which “the Constitution clearly spells out both a monetary remedy and even the necessary quantum of compensation due”).

130. *Id.* at 45.



Clause violations should be treated differently from other constitutional violations because of the compensation language expressly provided by the Fifth Amendment.<sup>131</sup>

#### D. *Addressing Other Contentions*

The Oversight Board raised three additional issues that the First Circuit addressed as minor points; the Oversight Board (1) noted that compensation claims are routinely affected by other areas of law without offending the Fifth Amendment, (2) highlighted that other constitutional provisions prescribe a remedy for compensation, and (3) asserted that allowing Takings Clause claims to be nondischargeable in bankruptcy would endanger the ability of municipalities to restructure in future Chapter 9 bankruptcies.<sup>132</sup> The First Circuit dealt with each in turn.

Firstly, the Oversight Board pointed to various instances where a claim for just compensation can go uncompensated without violating the Fifth Amendment.<sup>133</sup> Routinely, Takings Clause claims are time-barred by statutes of limitation, settled for less than full value, or waived by operation of contract and state law.<sup>134</sup> The court viewed this argument as a conflation of two separate categories of denial: substantive and procedural.<sup>135</sup> According to the court, procedural bounds like statutes of limitations are perfectly legitimate; setting a deadline for the initiation of legal action does not offend the Constitution.<sup>136</sup> The court dismissed waiver and settlement as “litigation decisions that a claimant has control over,” whereas a bankruptcy discharge takes away creditor control over the just compensation claim.<sup>137</sup>

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131. *See id.* (finding the dissenting opinion in *In re Stockton* to accord with the court’s interpretation of the Fifth Amendment guarantee). The court explains that the Takings Clause, by prescribing its own remedy as just compensation, is set apart from other constitutional claims that “lack an express basis in the Constitution” and can be adjusted in bankruptcy. *Id.* at 45–46; *In re City of Stockton*, 909 F.3d 1256, 1273 (9th Cir. 2018) (“Where a taking has occurred, just compensation is owed and cannot be reduced—bankruptcy notwithstanding. Accordingly, a municipality may not nullify its obligation to pay just compensation for seized property through a Chapter 9 proceeding. Rather, claims for just compensation should be excepted from discharge, such that they survive any bankruptcy intact.”).

132. *See In re Fin. Oversight*, 41 F.4th at 45–46.

133. *See id.* (“First, the Board argues that claims for just compensation are routinely modified by the operation of law after takings occur, all apparently without offending the Fifth Amendment.”).

134. *See id.*

135. *See id.* at 45 (drawing a line between “denial of just compensation” and “what may make a claim for just compensation procedurally inactionable or waivable by the claimant”).

136. *See id.*

137. *See id.* at 45–46 (dismissing the heart of the Oversight Board’s argument, namely that Takings Clause claims can be disposed of without providing just compensation, which would not violate the Constitution). The court did not suggest that there is a constitutional basis for treating a statute of limitation barring com-

Secondly, the Oversight Board pointed to § 1983 claims and Bivens claims as creating causes of action for damages “implied directly under the Constitution.”<sup>138</sup> The court reiterated its previous rationale for concluding that the Takings Clause is different because it *explicitly* prescribes the amount of compensation due.<sup>139</sup>

Lastly, the Oversight Board argued that a “parade of horrors” would stem from an affirmation of the lower court’s decision—chiefly that future municipal restructurings would be endangered if Takings Clause claims were categorically exempted from discharge.<sup>140</sup> The First Circuit was unpersuaded that public policy truly pushed in this direction.<sup>141</sup> Rather, the court found the greater concern to be that municipalities would have an incentive to effect takings, build up their just compensation obligations, and then seek to reduce or discharge them in bankruptcy.<sup>142</sup>

Having dealt with all the Oversight Board’s contentions, the First Circuit handed down its ruling. In affirming the lower court’s decision, the First Circuit held that any time the government takes private property, it is required to pay just compensation, meaning that the bankruptcy court was required to reject confirmation of a plan that would relieve the Commonwealth of those obligations.<sup>143</sup>

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pensation differently from a bankruptcy discharge, relying instead on First Circuit precedent regarding the rationale for statutes for limitations. *Id.*

138. *See id.* at 46 (quoting *Davis v. Passman*, 442 U.S. 228, 230 (1979)) (setting out the Board’s argument that other types of suits brought to enforce constitutional rights also find their basis in the constitution, but are adjusted in bankruptcy); *see also* Turner, *supra* note 61, at 4 (explaining that § 1983 does not apply to “[t]he federal government, its agencies, its officers or employees” because a “Bivens Claim provides a remedy against the federal government and its officials for constitutional violations”).

139. *See In re Fin. Oversight*, 41 F.4th at 46 (“Neither Bivens nor section 1983 rest on a provision of the Constitution that mandates a specific remedy in the same way the Takings Clause mandates just compensation.”).

140. *See id.*

141. *See id.* (deciding that “interpreting the law to create an incentive to pursue such a gambit strikes us as poor policy and certainly not a reason to adopt the Board’s position”).

142. *See id.* (hypothesizing that an unfortunate eventuality might be municipalities owing “a considerable amount of money to property owners for past takings and fil[ing] for bankruptcy in the hopes that it may leave the takings in place without paying anything like just compensation for the property”).

143. *See id.* (describing the issue as “rather simple” and holding that the lower court properly found that the plan could not be carried out if the Commonwealth was not required to pay its just compensation obligations).

V. ON CHOPPY WATERS: A CRITICAL ANALYSIS OF *IN RE FINANCIAL OVERSIGHT* AND THE FIRST CIRCUIT'S APPROACH TO EVALUATING THE DISCHARGEABILITY OF TAKINGS CLAUSE CLAIMS

The First Circuit's holding in *In re Financial Oversight* with its decision to apply Takings Clause protections to just compensation claims raises three issues. First, the continued reliance upon the *Radford* mantra that "[t]he bankruptcy power[ ] . . . is subject to the Fifth Amendment," came about by relying on inapposite precedent and is too rigid a rule to adapt to the changing landscape of Takings Clause jurisprudence.<sup>144</sup> Second, the First Circuit's rationale for refusing to discharge Takings Clause Claims is logically inconsistent given recent Supreme Court precedent in *Knick*.<sup>145</sup> Third, as the reach of the Takings Clause continues to grow, adherence to the *Radford* mantra will allow unintended claimants to use the Fifth Amendment's safe harbor to prevent discharge of their claims.<sup>146</sup>

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144. See *Louisville Joint Stock Land Bank v. Radford*, 295 U.S. 555, 589 (1935) (distinguishing the ability of Congress to discharge a debtor of personal liabilities and contractual obligations, and the constitutional limits on Congress forbidding them from taking substantive specific property rights); see also Rogers, *supra* note 27, at 978 (describing the academic debate surrounding secured creditors in bankruptcy). Rogers claims that "[v]irtually every discussion of the problem includes a reference to" the *Radford* mantra. *Id.* He further argues that "later cases overrule or substantially undercut the vitality of *Radford*." *Id.* at 981. He contends that *Radford* does not provide support for the assertion "that the fifth amendment imposes definite constitutional limitations on the substance of bankruptcy legislation." *Id.* Though secured creditors are different from takings claimants, Rogers' argument is nonetheless salient in attacking the relevancy of *Radford* generally; "*Radford* and its progeny, however, provide no support at all for the assertion of such a broad substantive limit on the powers of Congress under the bankruptcy clause." *Id.* at 984.

145. Compare *In re Fin. Oversight*, 41 F.4th at 44–45 (distinguishing Takings Clause claimants from civil rights claimants purely on the basis that the Fifth Amendment provides a textual remedy in the Constitution, while civil rights victims must pursue statutory causes of action), with *Knick v. Twp. of Scott*, 139 S. Ct. 2162, 2179 (2019) (suggesting the statutory remedy for a § 1983 action is the proper recourse for Takings Clause violations).

146. See Marissa A. Wiesen, *Chapter 9 Bankruptcy in Detroit and the Pension Problem*, 49 NEW ENG. L. REV. ON REMAND 25, 25–26, 31 (2014) (arguing that pensions should not be given special treatment over other unsecured claims). Wiesen addressed the issue of pensions in the Detroit bankruptcy, where tension rose as a result of the assertion that pensions were unimpairable under the Michigan Constitution. *Id.* at 31. Though a class of claims obtaining more protection by virtue of a state constitution is a slightly different issue than the issue discussed in this Note, it illustrates that future entitlements claims may receive more protection because they resemble property rights, which could make the claims immune from discharge. *Id.*

A. *Relying on the Wrong Precedent*

*Radford* properly invoked the Fifth Amendment to limit Congress's ability to wipe out a secured creditor's foreclosure rights through the bankruptcy process.<sup>147</sup> However, following the *Radford* decision, courts have continued to cite to it for its broad proposition that bankruptcy is generally subject to the Fifth Amendment.<sup>148</sup> In *Radford*, the Court intended to apply this limitation to Congress's bankruptcy power—namely, that bankruptcy statutes are not permitted to perpetually work a taking on creditors by operation of law.<sup>149</sup> The Court would go on to prevent the bankruptcy process from impairing certain property interests, like mortgage liens in real property or liens in personal property.<sup>150</sup> While such a rule preventing the impairment of these types of property interests may not be axiomatic, it has stood the test of time and courts continue to prevent dispossession of creditors' real property rights in bankruptcy proceedings.<sup>151</sup>

*In re Detroit* and *In re Stockton* represent the limited pool of federal cases that had addressed the precise question of whether prepetition just compensation claims can be discharged in bankruptcy, and while both the Detroit court and the Stockton dissent cited the *Radford* mantra, in neither case was Fifth Amendment protection dispositive.<sup>152</sup> Nevertheless, in *In re*

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147. See *Radford*, 295 U.S. at 589 (holding that Congress's attempt to use the bankruptcy process to strip citizens of their foreclosure rights without just compensation was a violation of the Fifth Amendment).

148. See *supra* Part II for a discussion of the line of cases interpreting and reiterating *Radford*; see also Forrester, *supra* note 27, at 866–88 (exploring *Radford* and its progeny, claiming that despite subsequent cases undercutting some of the details of *Radford*, “they do not call into question the principle that the bankruptcy power is subject to the Fifth Amendment”).

149. For a discussion of the facts of *Radford* and the original holding, see *supra* notes 46–50 and accompanying text.

150. See *United States v. Sec. Indus. Bank*, 459 U.S. 70, 74 (1982) (invoking *Radford* for the proposition that “[t]he bankruptcy power is subject to the Fifth Amendment’s prohibition against taking private property without compensation”); Forrester, *supra* note 27, at 866–70 (discussing *Radford* and the cases to follow that continued to guarantee that bankruptcy processes did not destroy mortgage lien rights for bondholders or lien on personal items perfected prepetition). For a discussion of the limitations that the Takings Clause places on bankruptcy proceedings, see *supra* notes 49–58 and accompanying text.

151. See 11 U.S.C. § 1129 (requiring that secured claims be paid the full value of their claim or allowed to keep lien rights intact for a plan to be confirmed); Forrester, *supra* note 27, at 877 (noting that some scholars take the normative view that secured creditors should not be treated differently than unsecured creditors, but “the Supreme Court has taken a different view”). Forrester elaborates, noting: The Bankruptcy Code definition of a lien includes an interest in property. Furthermore, the Supreme Court has recognized that a security interest is an interest in property. The law does treat and historically has treated the interest of a secured creditor in either real or personal property as an interest in the property.

*Id.* at 875.

152. See *supra* note 120 (discussing the decision of the *In re Detroit* court to adopt the reasoning of the United States Attorney General and avoid the constitu-

*Financial Oversight*, the First Circuit cited approvingly to the *In re Detroit* opinion and the *In re Stockton* dissent, and again invoked the *Radford* mantra, holding that discharging the Takings Clause claim would be unconstitutional.<sup>153</sup>

Paradoxically, in *In re Financial Oversight* the First Circuit discredited as “inapposite” several cases that the Oversight Board brought forward because those cases spoke to whether “bankruptcy law has effected a taking of property,” not the issue of whether discharging a just compensation claim would violate the Fifth Amendment.<sup>154</sup> Yet, the *Radford* mantra—and its progeny that rely on it—are *also* those “inapposite” cases dealing with bankruptcy law effecting a taking.<sup>155</sup> It is inherently inconsistent for the First Circuit to rely on *Radford* as precedent, a case having nothing to do with the discharge of just compensation claims, while choosing to disregard cases as “inapposite” for precisely that characteristic.<sup>156</sup>

Moreover, the First Circuit’s decision seems to treat creditors with various constitutional claims differently, while claiming it is not creating a constitutional creditor hierarchy.<sup>157</sup> The opinion stated that “[bank-

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tional issue by utilizing its discretion to exempt the claims from discharge pursuant to § 944(c)(1) of the Code). For further discussion on the decision by the *In re Stockton* court to invoke equitable mootness grounds to dispose of the case due to the plaintiff’s failure to raise issues in a timely manner rather than rule directly on the constitutional issue, see *supra* note 91 and accompanying text.

153. For a discussion of the First Circuit’s characterization of the Michigan bankruptcy court’s holding in *In re Detroit* and its decision to align itself with Judge Friedland’s dissent in the *In re Stockton* case, see *supra* notes 120, 121, 131, and accompanying text.

154. See *In re Fin. Oversight & Mgmt. Bd.*, 41 F.4th 29, 43 (1st Cir. 2022) (explaining the court’s disregard for cases brought to its attention by the Oversight Board, specifically stating *Kuehner* and other related cases are “only relevant if we assume that claims for just compensation are the same as any contractual claims for payments due” and declaring that “[c]ases that involve no impairment in bankruptcy of claims for just compensation shed no useful light” on the issue), *cert. denied* 143 S. Ct. 774 (2023).

155. See *id.* at 42 (asserting that on the relation of the Takings Clause to bankruptcy laws, “the Supreme Court has been very clear: The bankruptcy laws are subordinate to the Takings Clause”). For this proposition, the First Circuit signals to both *Radford* and *Security Industry*. *Id.*; Forrester, *supra* note 27, at 867 (describing the issue in *Radford* as one concerned with a mortgagee’s property rights and explaining that the Court held an act of Congress violated the Fifth Amendment). Forrester later describes the issue in *Security Industry* as whether a debtor could use a bankruptcy provision to avoid liens on the debtor’s furnishing and appliances. *Id.* at 869; Rogers, *supra* note 27, at 985 (arguing that if *Radford* has any precedential influence outside the specific act of Congress it was confronting, it should be narrow and limited to instances where “statutes that retroactively disrupt settled expectations may be subject to particularly attentive judicial scrutiny”).

156. See *In re Fin. Oversight*, 41 F.4th at 43 (disregarding several cases presented by the Oversight Board as “inapposite,” preferring to structure the question as “whether the denial of just compensation for such a taking violates the Fifth Amendment,” framing the inquiry so broadly and in exactly the terms of the Constitution).

157. See *id.* at 46 n.8 (“The Board contends that distinguishing among Takings Clause claims and other constitutional claims in this way somehow creates a

ruptcy] laws are not categorically exempt from the requirements of the Fifth Amendment (any more than they are exempt from, for example, the First Amendment),” suggesting that the many prohibitions found in the Constitution apply with equal force to bankruptcy law.<sup>158</sup> Though not a contentious position—bankruptcy laws cannot violate freedom of speech or impinge on the free exercise of religion—the court had no problem distinguishing First or Fourth Amendment protection, and finding remedies for these constitutional violation claims to be subject to discharge or impairment: “[N]othing in the Constitution itself specifies any particular remedy that must be provided when the government engages in a Fourth Amendment violation. Indeed, absent remedies provided for by statute or federal common law, there is no right to monetary relief for most constitutional violations.”<sup>159</sup> The court relegated this argument to a footnote, dismissing the contention that their ruling “creates a hierarchy among constitution rights” as unfounded.<sup>160</sup> Rather, the court viewed itself as “recognizing that such rights are safeguarded in different ways.”<sup>161</sup> It is difficult to understand how victims who have had their First or Fourth Amendment rights violated by a city and litigated their claims to judgment only to have those § 1983 claims discharged, will see their rights as “safeguarded in a different way,” while the Takings Clause claimant has their claim for a constitutional violation paid out in full.<sup>162</sup>

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‘hierarchy among[ ] constitutional rights.’ But we do not create a ‘hierarchy’ of constitutional rights simply by recognizing that such rights are safeguarded in different ways.” (quoting *Caplin & Drysdale, Chartered v. United States*, 491 U.S. 617, 628 (1989)). The Court points out that Bivens and § 1983 claims are “different in kind” from Takings Clause violations, and cites approvingly to *In re Stockton* for proposition that claims “under 42 U.S.C. § 1983 for money damages stemming from constitutional violations are “routinely adjusted in bankruptcy.” *Id.* at 45–46.

158. *See id.* at 42 (purporting to put the various constitutional protection on equal footing).

159. *Id.* at 44–45.

160. *See id.* at 46 n.8 (reiterating that their reasoning for treating the Fifth Amendment differently was due to the express provision within the text of the Amendment).

161. *See id.* (acknowledging the Oversight Board’s reference to the 1989 Supreme Court case *Caplin & Drysdale v. United States*, which the Board offered to support its contention that distinguishing among Takings Clause claims and other constitutional claims creates a “hierarchy among[ ] constitutional rights” (alteration in original) (quoting *Caplin*, 491 U.S. at 628)).

162. *Id.*; *see also* Jacoby, *supra* note 3, at 59 n.22 (noting that the Detroit bankruptcy resulted in “new law of dischargeability of civil rights claims and the nondischargeability of Takings Clause claims”); *In re City of Stockton*, 909 F.3d 1256, 1268 (9th Cir. 2018) (discrediting the assertion that a claim is protected because it is “founded as a constitutional claim” and commenting that § 1983 claims are often adjusted in bankruptcy). For a discussion of the treatment of civil rights claims in the Detroit bankruptcy, see *supra* note 13 and accompanying text.

Moreover, while the government is forbidden from ever violating most rights secured by the Constitution, the taking of private property is not even a violation so long as it is compensated.<sup>163</sup> If a “hierarchy” among constitutional rights *did* exist, why would Takings Clause claims occupy a more secure place in the bankruptcy?<sup>164</sup> One could suggest that the government should be *more* on the hook for acts that are clearly verboten—such as brutalizing its citizens, censoring speech, or depriving citizens of due process—as opposed to something like an uncompensated regulatory taking, a debatable constitutional violation.<sup>165</sup>

The First Circuit unnecessarily chained itself to the rock of *Radford* in deciding this case.<sup>166</sup> Whether it would be more to the public good to find all claims for constitutional violations dischargeable or nondischargeable is unclear, but the inconsistencies that result from the court’s clinging to the outdated and “inapposite” precedent of the *Radford* mantra is surely not the way forward.<sup>167</sup>

#### B. *Supreme Court and Knick*

Additionally, the court refused to find *Knick* relevant to this issue of the dischargeability of takings claims.<sup>168</sup> *Knick* overturned long-standing doctrine that a claimant could not pursue a federal remedy for just com-

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163. Compare U.S. CONST. amend. I (placing a clear restriction on government, requiring that “Congress shall make no law respecting an establishment of religion, or prohibiting the free exercise thereof; or abridging the freedom of speech, or of the press; or the right of the people peaceably to assemble, and to petition the Government for a redress of grievances”), with U.S. CONST. amend. V (conditioning government action; “[N]or shall private property be taken for public use, without just compensation”).

164. See U.S. CONST. amend. V (text indicating the conditional nature of a Takings Clause violation based on lack of compensation). For a discussion of the First Circuit’s disagreement with the Board asserting that its holding would create a “hierarchy” amongst constitutional rights, see *supra* note 157–162 and accompanying text.

165. See *supra* note 163 (comparing the text of the First and Fifth Amendment); Gold, *supra* note 37, at 187 (arguing that the meaning of “taken” in the Fifth Amendment is subject to reasonable disagreement and noting that one interpretation of the Takings Clause is that it never protects citizens from regulatory takings). Gold also suggests that the original intent of the Takings Clause is unknown and we are ultimately left with the “Supreme Court’s case-by-case handling” of takings issues. *Id.* at 185.

166. See *In re Fin. Oversight*, 41 F.4th at 42 (buttressing its holding with the unequivocal statement that bankruptcy laws are subordinate to the Takings Clause).

167. For a detailed discussion of the historical interaction between the Takings Clause and bankruptcy, as well as the difficulties in continuing to apply a rigid rule to Takings Clause claims in bankruptcy proceedings, see *supra* Part II.

168. See *In re Fin. Oversight*, 41 F.4th at 43 (accusing the Oversight Board of “overreading” *Knick*). The court believed that *Knick* casted no doubt on the decree that just compensation must be paid. *Id.* Rather, the court reasoned that a Takings Clause violation may vest at the time of the taking and a subsequent denial of compensation through the bankruptcy process may also give rise to “Fifth Amendment concerns.” *Id.*

pensation until State remedies had been exhausted.<sup>169</sup> In doing so, *Knick* opened the federal courthouse to takings victims the moment the uncompensated taking had occurred, stating that a property owner could immediately bring a § 1983 claim upon having property taken.<sup>170</sup> This holding creates tension with the inchoate *In re Detroit* doctrine that § 1983 claims are dischargeable, while Takings Clause violations are not.<sup>171</sup> With the Supreme Court suggesting federal takings claims may proceed through § 1983, the next court to deal with a large municipal bankruptcy will be faced with complex problems.<sup>172</sup> Will that court be forced to sort the dischargeable from nondischargeable § 1983 claims or perhaps determine what amount of a particular § 1983 claim is for just compensation rather than compensation for the constitutional violation?<sup>173</sup>

Moreover, the proclamation from *In re Stockton* that § 1983 claims are dischargeable in municipal bankruptcy is still unchallenged in appellate courts.<sup>174</sup> In *In re Detroit*, the § 1983 claims were discharged against the

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169. For a discussion of *Knick* and the precedent it overturned, see *supra* Section II.C.

170. See *Knick v. Twp. of Scott*, 139 S. Ct. 2162, 2168 (2019) (holding that victims of a Takings violation may bring a claim in federal court immediately upon the uncompensated taking, regardless of other forms of recourse, stating, “The property owner has suffered a violation of his Fifth Amendment rights when the government takes his property without just compensation, and therefore may bring his claim in federal court under §1983 at that time”).

171. For a discussion of the unprecedented decision to treat the dischargeability of these two constitutional claims differently in the Detroit bankruptcy, see *supra* notes 79–82 and accompanying text.

172. See *Turner*, *supra* note 61, at 8 (listing the Fifth Amendment’s guarantee of just compensation for takings as a constitutional right enforceable under § 1983); *In re City of Detroit*, 524 B.R. 147, 262–71 (Bankr. E.D. Mich. 2014) (committing eight pages of the opinion to parsing and evaluating the potential impairment of civil rights and takings claims); Brian T. Hodges, *Knick v. Township of Scott, PA How a Graveyard Dispute Resurrected the Fifth Amendment’s Takings Clause*, 60 SANTA CLARA L. REV. 1, 21 (2020) (arguing that even if the government pays just compensation at a later time, a constitutional violation still occurred). Hodges also explains that prior to *Knick*, would be federal takings claimants would have to bring their claim in state court and then remove it to “federal court under 28 U.S.C. § 1441 on the basis that it raises a ‘federal question.’” *Id.* at 18 (citing *Int’l Coll. of Surgeons*, 522 U.S. 156, 164 (1997)).

173. Compare *In re City of Stockton*, 909 F.3d 1256, 1268 (9th Cir. 2018) (stating that § 1983 claims are routinely discharged in bankruptcy), with *Knick*, 139 S. Ct. at 2168 (holding that Takings Clause violation victims can bring §1983 claims immediately upon the uncompensated taking). See also *Knick*, 139 S. Ct. at 2172 (stating that “later payment of compensation may remedy the constitutional violation that occurred at the time of the taking, but that does not mean the violation never took place”). The Court goes on to specify the relief and legal action available to the victim, stating “someone whose property has been taken by a local government has a claim under § 1983 for a “deprivation of [a] right[ ] . . . secured by the Constitution” that he may bring upon the taking in federal court.” *Id.*

174. See *In re Stockton*, 909 F.3d at 1263–66 (finding all analytical factors in support of dismissal due to equitable mootness). See generally *In re City of Detroit*, 524 B.R. 147, 270 (Bankr. E.D. Mich. 2014) (utilizing the Bankruptcy court’s equitable powers and principals of constitutional avoidance to avoid confronting the



city, but they were not discharged against *individual* state actors.<sup>175</sup> That is, the claims for various civil rights and Fourth amendment violations were discharged against the City of Detroit, but remained intact against the individual city officials who had committed the violations.<sup>176</sup> Because the city had an obligation to defend and indemnify civil rights claims against city officers, the “economic reality behind this” was that the city was still the de facto defendant and would inevitably foot the bill for any later successful claims against the individuals.<sup>177</sup>

Again in *In re Stockton*, the court stated “§ 1983 claims[ ] are routinely adjusted in bankruptcy,” suggesting the commonplace nature of such discharges.<sup>178</sup> Though § 1983 discharges are common in bankruptcy proceedings as a whole, nothing is routine about these large, modern Chapter 9 filings.<sup>179</sup> Indeed, *In re Detroit* was the first federal case to address the dischargeability of § 1983 claims in Chapter 9 bankruptcy proceedings; consequently that court’s analysis was based in large part on the U.S. Attorney General’s suggestions about the constitutionality of such a discharge.<sup>180</sup> What the *In re Stockton* court likely meant was that § 1983

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Fifth Amendment issue). The court specifically ruled on Takings Clause violation claims pursuant to its Section 944(c)(1) powers, rather than answering the constitutional question of discharging takings claims head-on; that decision was not reviewed on appeal. *Id.*

175. See *In re Detroit*, 524 B.R. at 265–66 (finding that the Code did not provide for the discharge of civil rights claims against individual officers). Detroit sought to have claims against both the city and individual officers discharged, but the court did not oblige, writing “a claim against a City official is not essentially one against the City for bankruptcy discharge purposes, even if state law requires the City to indemnify the official.” *Id.* (quoting *V.W. ex rel. Barber v. City of Vallejo*, No. CIV.S-12-1629, 2013 WL 3992403, at \*6 (E.D. Cal. Aug. 2, 2013)). The court then recognized that this would effectively result in that class of creditors being paid in full. *Id.* at 266. Thus, post-confirmation, the affected victims could expect their claims to be indemnified, and no impetus existed for challenging the dischargeability of such claims against the city itself. *Id.*

176. See *id.*

177. See *id.*

178. See *In re Stockton*, 909 F.3d at 1268 (disagreeing with Cobb’s arguments for constitutional protection of his claims and stating that constitutional based claims are routinely adjusted in bankruptcy). Cobb attempted to marshal *Radford* in defense of his position that his just compensation claim could not be adjusted, but the court instead found his claim more like certain secured interests that can be affected by the bankruptcy process—like lien rights. *Id.*

179. See Clayton P. Gillette & David A. Skeel Jr., *Governance Reform and the Judicial Role in Municipal Bankruptcy*, 125 YALE L.J. 1150, 1152, 1183–84 (2016) (noting that there are a rising number of Chapter 9 filings, but that “substantial municipalities[ ] make up a small fraction of [these] Chapter 9 [filings]”). Gillette and Skeel discuss the rising number of Chapter 9 filings, but the limited number of “substantial” filers. *Id.* at 1184. The majority of Chapter 9 filings are still small districts or municipal services. *Id.* at 1152.

180. See *In re Detroit*, 524 B.R. at 262, 268 (relying on the recommendations of the United States Attorney General that discharging Takings Clause violation claims would raise substantial constitutional concerns). Though the court used the subheading “Discharging Takings Clause Claims would violate the Fifth Amendment,” the actual text suggested that it elected to agree with the Attorney

claims *against individuals* are routinely adjusted in bankruptcy; that is, when an individual acting under the authority of state law receives an adverse § 1983 judgment, that individual may enter into a Chapter 7 or Chapter 13 bankruptcy, where that claim may be discharged.<sup>181</sup> However, individuals are not generally bound to constitutional standards—federal and state entities are.<sup>182</sup> While § 1983 may simply provide another cause of action for interpersonal legal judgments—similar to judgments under state negligence law or for breach of contract—it does not necessarily follow that a § 1983 judgment can be treated the same way in the context of a municipal bankruptcy.<sup>183</sup> The Supreme Court, in *Knick*, signaled its view that constitutional rights are all on equal footing, with vindication coalescing into the § 1983 action; however, the First Circuit seemed to disagree with this indication by allowing Fifth Amendment violations to be treated in a more privileged manner than other civil rights violations.<sup>184</sup>

### C. *Safe Haven Problem*

The third issue related to the claims that were *not* given Fifth Amendment protection in the plan, the two classes of plaintiffs that were denied just compensation for their claim: bondholders and Suiza Dairy.<sup>185</sup> The lower court opinion suggests that both groups had their claims impaired

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General's recommendation so that the court avoided the constitutional concern raised by utilizing its discretion to exempt the Takings Clause claims from discharge pursuant to § 944(c)(1). *Id.* at 262, 268.

181. *See, e.g., In re Nifong*, No. 08-80034C-7D, 2008 WL 2203149 (Bankr. M.D.N.C. May 27, 2008) (finding a Chapter 7 debtor subject to eight claims under 42 U.S.C. § 1983 and that such claims were not entitled to any immunity from discharge; rather that the burden was on the movants to show § 1983 claims could be exempted under the standards of 11 U.S.C. § 523—like other unsecured claims).

182. *See* ERWIN CHERMINSKY, CONSTITUTIONAL LAW: PRINCIPALS AND POLICIES 533 (6th ed., 2019) (stating that the Constitution applies to the government at all levels, including federal, state, and local governments, and to the actions of government officers at these levels). However, the Constitution does not generally apply to private entities or actors. *Id.*

183. *See* Laura N. Coordes, *Formalizing Chapter 9's Experts*, 116 MICH. L. REV. 1249 (2018) (asserting that Chapter 9 bankruptcies are challenging because of the need to apply generalized standards to “wildly different, specialized entities”). Judges must rely on standards imported from elsewhere in the Code, often chapter 11. *Id.* at 1250. Both because the standards originate in other parts of the Code and the dearth of large precedential municipal bankruptcies, the confirmation standards of Chapter 9 give “less protection, for both debtors and creditors.” *Id.* at 1251–55.

184. *See Knick v. Twp. Of Scott*, 139 S. Ct. 2162, 2167 (2019) (holding that § 1983 claims vest and can be pursued the moment an uncompensated taking occurs); *In re Fin. Oversight & Mgmt. Bd.*, 41 F.4th 29, 41–45 (1st Cir. 2022) (holding that the Fifth Amendment prevents the impairment of just compensation claims but also states that “claims under 42 U.S.C. § 1983 for money damages stemming from constitutional violations” can be impaired), *cert. denied* 143 S. Ct. 774 (2023).

185. *See In re Fin. Oversight & Mgmt. Bd.*, 637 B.R. 223, 299–300 (D.P.R. 2022) (discussing the treatment of bondholders that had invested in public utilities and brought forth a regulatory taking claim arguing that discharge would work

in the bankruptcy plan and were treated like any other unsecured creditor, despite raising Fifth Amendment concerns about this impairment.<sup>186</sup> Of particular importance, Suiza Dairy had entered into a settlement agreement with the municipality due to regulatory action that could have given rise to an inverse condemnation claim.<sup>187</sup> Presumably, Suiza Dairy could have litigated its claim directly and received a judgment awarding just compensation, a claim like those the First Circuit found were constitutionally protected from discharge.<sup>188</sup> However, whether it was on account of efficiency or practicality, the claim was settled and the government agreed to pay a sum on regular intervals as compensation for the regulatory action.<sup>189</sup>

The disparity in treatment of similar claims presents an issue of fairness between similarly situated claimants.<sup>190</sup> The lower court drew a line between the claim brought by Suiza Dairy, a settlement predicated on a taking, and other takings claims.<sup>191</sup> The First Circuit was then unpersuaded by the Oversight Board's argument that because Takings Clause claims could be waived or settled without offending the Fifth Amendment,

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as a taking and explaining that Suiza Dairy had entered into a stipulation as part of a regulatory scheme prior to fully adjudicating their just compensation action).

186. *See id.* at 298–300 (allowing the impairment of bondholders' and Suiza Dairy's claims). The court applied the *Penn Central* test to determine that the plan did not result in an unconstitutional taking from the bondholders. *Id.* at 299. The court found that Suiza Dairy was only entitled to contractual payment, which was entered into as part of a stipulation prior to adjudication of a regulatory taking claim. *Id.*

187. *See id.* at 299–300.

188. *See Vaqueria Tres Monjitas, Inc. v. Irizarry*, 587 F.3d 464, 468–69 (1st Cir. 2009) (utilizing an equitable remedy to settle dispute between Suiza Dairy and government regulatory action). Regulations were put in place that set a ceiling on the price of processed milk and a floor on how much Suiza Dairy was forced to pay farmers. *Id.* at 469; *see also In re Fin. Oversight*, 637 B.R. at 300 (characterizing the First Circuit's affirmation of the remedy as "equitable" rather than just compensation for a taking). The government entered into a contractual agreement to pay Suiza Dairy based on economic calculations through court-approved settlement. *Vaqueria*, 587 F.3d at 469.

189. *See* Brief for Appellant Suiza Dairy, Corp. at 10–12, *In re Fin. Oversight & Mgmt. Bd.*, 41 F.4th 29 (1st Cir. 2022) (No. 22-01119) (arguing that the Puerto Rican government remains a Taking Clause debtor for the purposes of their settlement agreement), *cert. denied* 143 S. Ct. 774 (2023). Suiza Dairy alleges that in 2013, it entered into a settlement agreement with the government to resolve a years-long dispute over milk regulation which provided that the government would pay hundreds of millions of dollars to compensate Suiza Dairy for lost profits resulting from the regulatory scheme. *Id.* at 5, 12.

190. *See* 11 U.S.C. § 1122(a) (2018) (instructing that "a plan may place a claim or an interest in a particular class only if such claim or interest is substantially similar to the other claims or interests of such class").

191. *See In re Fin. Oversight & Mgmt. Bd.*, 637 B.R. 223, 299–300 (D.P.R. 2022) (distinguishing Suiza Dairy's claim as "[u]nlike the objecting holders of Eminent Domain/Inverse Condemnation Claims" and failing to supply a "factual or legal basis for its assertion that it holds a valid Takings Clause Claim that is protected by the Fifth Amendment").

there was no constitutional problem with discharging those claims in bankruptcy.<sup>192</sup> The First Circuit found it to be significant that waiving a claim or failing to bring the claim in a timely manner are voluntary decisions, making them different from the compulsory impairment a bankruptcy discharge would have on victims of Takings Clause violations.<sup>193</sup> However, this line drawing between claims may lead to disparate treatment for those who decide to receive compensation via settlement agreements or payment plans, foregoing a complete adjudication of their takings claim.<sup>194</sup> The First Circuit holding means that these alternative compensation methods can be discharged in bankruptcy, despite the Fifth Amendment's command for just compensation impelling the settlement.<sup>195</sup>

#### VI. SAFE HARBOR OR OPEN WATER?: WHAT *IN RE FINANCIAL OVERSIGHT* MEANS GOING FORWARD

It is important to note that the proceeding in *In re Financial Oversight* took place under PROMESA, not the Bankruptcy Code.<sup>196</sup> While the provisions of PROMESA adopted much of the Code, and many aspects of the bankruptcy are derived from Chapter 9, it is possible that the holdings from the Puerto Rican bankruptcy will not largely affect precedent for future municipal bankruptcies.<sup>197</sup>

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192. See *In re Fin. Oversight*, 41 F.4th at 45–46 (dismissing the Oversight Board's argument as insufficient because "compliance with a statute of limitations, along with the choice of whether to waive or settle a claim, are litigation decisions that a claimant has control over. The impairment or discharge in bankruptcy of that claimant's entitlement to just compensation is not").

193. See *id.*

194. For a discussion of the alternative avenue of compensation Suiza Dairy entered into and their subsequent denial of constitutional protection from discharge, see *supra* notes 185–191.

195. See *In re Fin. Oversight*, 637 B.R. at 299 (rejecting Suiza Dairy's argument that its claim had constitutional protection). Suiza Dairy had brought a Takings Clause claim against the government but "prior to receiving final judgment on its . . . claim" the parties entered into the Suiza Dairy Producer Settlement. *Id.* This settlement required the government to follow certain formulae in paying compensation, but also functioned as "a final and unappealable judgment dismissing the action with prejudice." *Id.* at 299–300. This led the court to find this payment plan was "not just compensation for a taking" but merely "a contract-based claim for payment." *Id.* at 300.

196. See Skeel, *supra* note 76, at 863–84 (describing PROMESA and its origin and purpose).

197. See *id.* at 873 ("Title III [of PROMESA] is very similar to bankruptcy . . . . [T]heir eyes were on Chapter 9 when they constructed Title III."); Coordes, *supra* note 183, at 1257–58 (describing how Chapter 9, when it does import standards from other portions of the code, often must change or adapt that precedent because it was not designed for the Chapter 9 context). Additionally, municipalities are often idiosyncratic entities requiring "relief that is tailored to their unique situation." *Id.* at 1253. Puerto Rico is a highly unique municipal debtor as it is the "largest government bankruptcy in U.S. history." *Id.*

Additionally, the Supreme Court has declined to review the First Circuit's decision, but future Chapter 9 filings may deepen this circuit split.<sup>198</sup> Currently, the First Circuit stands as the lone circuit preventing the discharge of takings claims, though the Eastern District of Michigan bankruptcy court has taken the same stance.<sup>199</sup> Alternatively, the Ninth Circuit, in the *In re Stockton* case, is the only circuit that did allow for the discharge of a Takings Clause claim.<sup>200</sup> The unusual facts of the Stockton case allow for a narrow reading of that holding, however, making it possible that a more direct uncompensated takings discharge issue would have been evaluated differently.<sup>201</sup> As more cases present, a clear majority rule may emerge amongst the Circuits.

While the opportunity for application of these varied viewpoints on the issue is limited, the monetary implications of the split for takings creditors are weighty.<sup>202</sup> Chapter 9 filers have little control over which federal circuit they file in and thus takings creditors have no say about the prece-

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198. See *Fin. Oversight & Mgmt. Bd. for P.R. v. Coop. de Ahorro y Credito Abraham Rosa*, 143 S. Ct. 774 (2023) (denying the petition for writ of certiorari); Am. Bankr. Inst., *First and Ninth Circuit Split on Discharge of Takings Clause Claims*, ROCHELLE'S DAILY WIRE (July 21, 2022), <https://www.abi.org/newsroom/daily-wire/first-and-ninth-circuits-split-on-discharge-of-takings-clause-claims> [permalink unavailable] (describing the current split between the First and Ninth circuit as "not yet entrenched").

199. See *In re Fin. Oversight & Mgmt. Bd.*, 41 F.4th 29, 46 (1st Cir. 2022) (concluding broadly that Takings Clause claims cannot be discharged rather than limiting its holding to PROMESA context), *cert. denied* 143 S. Ct. 774 (2023). Also, the case explicitly dealt with *In re Stockton* and cited approvingly the *In re Detroit* case, suggesting the First Circuit was looking to Chapter 9 precedent and setting such precedent itself. *Id.* at 46.

200. For a discussion of the facts and holding by the Ninth Circuit in the Stockton bankruptcy, see *supra* notes 83–94 and accompanying text.

201. See *In re City of Stockton*, 909 F.3d 1256, 1260–69 (9th Cir. 2018) (explaining that the unusual facts underlying Cobb's claim in the Stockton bankruptcy only dealt with a single individual with an old contingent claim for just compensation beyond the set aside amount he had already been paid, suggesting that the state mechanism relieving Cobb of property rights was enough to make his claim unsecured, and that the timing of his claim and equitable nature of the remedy made its factual application narrow). Additionally, the case drew a dissent from Judge Friedland. *Id.* at 1269 (Friedland, J. dissenting).

202. See Brief for Appellant Suiza Dairy, Corp. at 19, *In re Fin. Oversight*, 41 F.4th 29 (No. 22-01119) (describing the size of the settlement agreement regarding the regulatory action affecting Suiza Dairy). Two claimants reached settlement for an accrual payment totaling \$170,639,638 that was not given protection under the Takings Clause. *Id.*; see also *In re Stockton*, 909 F.3d at 1262 (listing the value of Cobb's proof of claim at \$4.2 million).

dent that will apply to their claim.<sup>203</sup> However, Chapter 9 filings are so dispersed and unpredictable, it is hard to tell how long it could take for the circuit split to significantly deepen.<sup>204</sup>

A. *Prudent Contract Drafting in Takings Clause Claims Situations*

Regardless of whether other federal appellate courts side with the First or Ninth Circuit on this issue, there will always be pressure on Takings Clause creditors, like all creditors, to structure their debts to survive a bankruptcy.<sup>205</sup> Depending on where a municipal bankruptcy takes place, having an intact Fifth Amendment claim as a creditor may or may not result in a constitutionally protected path to escape the effects of a discharge.<sup>206</sup> In the First Circuit, claimants who waive their Fifth Amendment guarantee to just compensation through a settlement or payment plan with the government must be mindful that such a claim will likely be

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203. See 11 U.S.C. § 921 (2018) (controlling Chapter 9 bankruptcy petitions). Section 921(b) specifies, “The chief judge of the court of appeals for the circuit embracing the district in which the case is commenced shall designate the bankruptcy judge to conduct the case.” *Id.*

204. See Am. Bankr. Inst., *supra* note 198 (suggesting that if the Supreme Court had weighed in on this issue, the effects would be limited to Chapter 9 municipal bankruptcies and have little effect on consumer bankruptcies and corporate restructuring).

205. See Sleeper, *supra* note 7, at 120–32 (discussing the legal effects of the discharge and statutory means by which creditors can demonstrate their debt is excepted). If a debtor can obtain a discharge through bankruptcy, it avoids any liability on discharged debt and functions as a permanent injunction against collection attempts on the debt. *Id.* at 120. Section 727 of the Code provides for the discharge so long as the debtor does not satisfy one of the grounds for discharge. *Id.* at 116. However, § 727 requires an interested party, likely a creditor, to demonstrate that the debtor should not qualify for a discharge, though this can be difficult. *Id.* For example, to demonstrate that a debtor should not receive a discharge pursuant to § 727(a)(2) for a fraudulent transfer, “the creditor bears the burden of proof” and the “provision is to be construed liberally in favor of the debtor and strictly against the creditor.” *Id.* at 116–17. Section 523 of the Code gives statutory means for creditor to make a particular debt excepted from the discharge and provides nine grounds for an exception. *Id.* at 121–22. Grounds for exception include, among others, fraud, alimony obligations, and debts for willful and malicious injury. *Id.* For a discussion of the benefits secured loans have over unsecured loans in the bankruptcy process, see *supra* note 10 and accompanying text.

206. Compare *In re Stockton*, 909 F.3d at 1269 (failing to seek a stay resulted in a just compensation claim being labeled unsecured and adjusted), with *In re Fin. Oversight*, 41 F.4th 45 (distinguishing statutes of limitations, waiver, or settlement plans as constitutionally acceptable procedures by which a Takings Clause violation victim may lose their right to compensation).

treated as an unsecured contract right, rather than a protected Fifth Amendment claim.<sup>207</sup> It is only now, *ex post*, that claimants like Suiza Dairy fully realize the ramification of such a waiver.<sup>208</sup>

Individuals and their representation must be aware that pursuing a court judgment for just compensation and agreeing to payment outside court may not be treated alike in bankruptcy.<sup>209</sup> It may be wise for takings victims to structure any negotiated settlement with municipal entities so that they receive a security interest or funds promptly, or find a way to ensure that their Fifth Amendment protection has not been waived if the municipality ends up in bankruptcy.<sup>210</sup>

### B. *Expanding Safe Harbor*

Perhaps the most significant aspect of *In re Financial Oversight* will be its effect on future debt obligations for entities that can make use of Chapter 9 filings.<sup>211</sup> Assuming that the First Circuit stands pat in its decision, or doubly so if the Supreme Court ever takes up the issue and sides with the First Circuit, there will be a major incentive for creditors to work their way into the sphere of Fifth Amendment protection.<sup>212</sup>

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207. See *In re Fin. Oversight*, 41 F.4th at 45–46 (separating denial of compensation from “what may make a claim for just compensation procedurally inactionable or waivable”); *In re Fin. Oversight & Mgmt. Bd.*, 637 B.R. 223, 300 (D.P.R. 2022) (recounting that prior to the bankruptcy, as a result of settlement with the government, “there was no favorable adjudication of Suiza’s Takings Clause claim” and accordingly, Suiza Dairy “merely has a contract-based claim for payment pursuant to the . . . Settlement”).

208. For a discussion of Suiza Dairy’s claim that was impaired in the bankruptcy process, see *supra* notes 185–189, 202, and accompanying text.

209. For further discussion on the claims brought bondholders and Suiza Dairy asserting Takings Clause violations that were ultimately determined to be adjustable, see *supra* notes 185–186, and accompany text.

210. See *In re Fin. Oversight*, 637 B.R. at 299–300 (deciding to forego adjudication on the merits of the Takings Clause claim and instead accepting settlement). Because there was no final adjudication on the merits of whether a taking had occurred, the settlement was characterized as “an equitable remedy,” resulting in the payment of monies, not compensation for a taking. *Id.* Moreover, the settlement explicitly provided that once it was court approved, it would operate as a final judgment on the matter and the action would be dismissed with prejudice. *Id.*

211. See MoloLamken LLP, *Does the Takings Clause of the U.S. Constitution Require the Government to Compensate Businesses for Forced Temporary Closures?*, <https://www.mololamken.com/knowledge-Does-the-Takings-Clause-of-the-U-S-Constitution-Require-the-Government-to-Compensate-Businesses-for-Forced-Temporary-Closures> [https://perma.cc/9UHX-XNWM] (last visited May 15, 2023) (suggesting that in the wake of COVID-19 executive orders that mandated closures, or required hotels or medical facilities to be used in particular ways, might be takings). This could pose issues for the most vulnerable municipalities that turn to takings-like measures during emergencies or pandemics and end up in Chapter 9 without a way to restructure huge obligations that are naturally coextensive with the cause of their filing. *Id.*

212. See *In re Fin. Oversight*, 41 F.4th at 46 (holding that a bankruptcy plan could not be confirmed without violating the constitution if the plan sought to

Bondholders, pensioners, victims of government regulatory schemes, and creditors of any kind will be incentivized to find creative methods to protect their debts from discharge.<sup>213</sup> If courts are willing to extend the reach of the Fifth Amendment, and also view it as an absolute bar to bankruptcy impairment, the class of constitutionally protected claims that can flourish under the Takings Clause may grow as far as normative argument and innovative lawyering allows.<sup>214</sup> As cities become more ready to utilize Chapter 9, any future economic downturn, paired with shaky municipal pension structures, will likely implicate the Takings Clause doctrine at issue here, and is sure to have profound and lasting effects on the treatment of the government's creditors, large and small.<sup>215</sup>

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impair claims for just compensation). For a discussion of dischargeability and the benefits of excepting a debt from discharge as a creditor, see *supra* note 205.

213. See Jeffrey B. Ellman & Daniel J. Merrett, *Pensions and Chapter 9: Can Municipalities Use Bankruptcy to Solve Their Pension Woes?*, 27 EMORY BANKR. DEV. J. 365, 371 (2011) (suggesting that Chapter 9 is available as an answer to the debt loads faced by many United States municipalities and future litigation will certainly raise thorny questions over the impairment of such obligations).

214. See *In re Fin. Oversight*, 41 F.4th at 46 (noting that the Board anticipates a “parade of horrors” will ensue as more obstacles are placed in the way of cities and municipalities being able to restructure their debts); Petition for a Writ of Certiorari at 1–4, *In re Fin. Oversight*, 41 F.4th 29 (No. 22-367) (noting the number of municipal debtors in recent years, the significant just compensation debt they carry, and arguing against the unprecedented holding by the First Circuit). Specifically, the petition notes that “one hundred seventy governmental debtors” filed for bankruptcy since 2000, and “unsecured claims for just compensation comprise a significant portion of the claims against” them. *Id.* at 2. The Board argues that if municipalities are unable to adjust these debts, they “may find themselves unable to restructure their debts” and they will find themselves in excessive litigation as “claimholders recast their claims as ‘takings’ that are immunized from discharge by the Fifth Amendment.” *Id.* at 23; see also Eric Kades, *The Natural Property Rights Straitjacket: The Takings Clause, Taxation, and Excessive Rigidity*, 51 U.C. DAVIS L. REV. 1351, 1357–59 (2018) (exploring the position of natural rights theorists in the scholarly debate over what constitutes property for purposes of the Takings Clause). Natural rights theorists advocate for an expansive reading of constitutional property protection to guard against overreaching legislative action. *Id.* at 1357. Kades identifies a particular theorist’s views that the Takings Clause’s guarantee of just compensation goes so far as to include taxation; that is, the citizenry is taxed in exchange for just compensation in the form of public services. *Id.* For a discussion of the variety of types of property that have received Takings Clause protection outside the bankruptcy context, see *supra* notes 44–48 and accompanying text.

215. See generally Gillette & Skeel Jr., *supra* note 179 (commenting on the increasing number of Chapter 9 filings and the benefits municipalities seek to gain from a restructuring); see also Ellman & Merrett, *supra* note 213, at 367 (identifying a major issue facing municipalities to be a “dramatic and growing shortfall in public pension funds”). The deficit faced by state pension and municipalities participating in those funds “is estimated by some to exceed \$3 trillion nationwide.” *Id.* Ellman and Merrett identify Chapter 9 as a potential road to relief for these municipalities. *Id.* at 370.



