When the Taker Goes Broke: Takings Claims in Municipal Bankruptcy

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When a municipality takes property, the former owners can allege a violation of the Takings Clause and try to recover just compensation. But what should happen when the municipality goes broke and enters municipal bankruptcy? Can the municipal Bankruptcy Code empower judges to release municipalities from their obligation to pay just compensation through a discharge? Or does the Takings Clause provide special constitutional protection to claims for just compensation from a municipality that immunizes the claims from discharge? This issue has played out in municipal bankruptcies in Detroit, Michigan; Stockton, California; and Puerto Rico—and courts are deeply divided on the right approach. There now is a live circuit split over the issue: the Ninth Circuit has held that takings claims receive no special protections from discharge, whereas the First Circuit has held that takings claims do receive constitutional protection.

This Comment provides the first comprehensive analysis that shows that takings claims are constitutionally dischargeable. As a threshold matter, the Comment shows that formalist considerations do not require immunizing takings claims from discharge. Even if the Takings Clause directly creates a right to recover just compensation, the right to recover just compensation from a municipality can be discharged without improperly infringing on the constitutional right. The Comment then shows that making takings claims dischargeable follows best from the original design of the Takings Clause given the host of procedural and political safeguards within municipal bankruptcy that would protect takings claimants against abuse. Lastly, the Comment shows that making takings claims dischargeable is normatively good. This position helps keep municipal bankruptcy relatively accessible and avoids creating thorny doctrinal problems. Even those with takings claims have minimal grounds to object to their claims being dischargeable given that they will generally be made no worse off by the municipal bankruptcy regime as a whole.

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INTRODUCTION

In 2013, Detroit went bankrupt. At the time, the City of Detroit faced $18 billion in debt and made history as the largest municipality in the United States to file for bankruptcy.[1] Detroit filed its first plan—its proposal to adjust its outstanding liability—in February 2014.[2] It had no settlements from any of its creditors, with "nearly every creditor group" filing litigation against the City to seek "the full protection of [their] claims."[3] By October, Detroit had reached settlements with nearly every represented creditor group.[4] Detroit's plan seemed well on track to approval, with the City on the verge of reducing its liability by over $7 billion[5] and getting "the fresh start that it need[ed] and deserv[ed] under our federal bankruptcy laws."[6]

But Detroit's plan faced potential problems from one group of creditors who resisted the bankruptcy plan and insisted they were entitled to the full value of their constitutional claims

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1 Quinn Klinefelter, *10 Years Ago Detroit Filed for Bankruptcy. It Makes a Comeback but There Are Hurdles*, NPR (July 22, 2023), https://perma.cc/T29V-8R5N.

2 *See In re* City of Detroit, 524 B.R. 147, 160 (Bankr. E.D. Mich. 2014).

3 *Id.*

4 *Id.*

5 *Id.* at 162.

6 *Id.* at 277.

against the City.[7] Many of these "creditors with constitutional claims," as the court labeled them,[8] were litigating civil rights claims against Detroit under 42 U.S.C. § 1983 and related statutes.[9] These creditors sought to recover damages from the City for excessive use of force, wrongful conviction arising from due process violations, and other constitutional violations.[10] In addition, three organizations had raised claims against Detroit under the Takings Clause[11] for property allegedly taken without just compensation.[12] The claims focused on Detroit's opportunistic practices to acquire property at an artificially low value in advance of expanding its airport.[13] Detroit's bankruptcy plan would largely release the City from liability for both kinds of constitutional claims through a process known as "discharge."[14] The civil rights and takings creditors alike would only be able to recover 10–13% of the face value of their claims against the City after their claims were discharged.[15] The court overseeing Detroit's bankruptcy found no constitutional problems with the plan's discharge of the civil rights creditors' claims, letting them recover only cents on the dollar.[16] On the other hand, the court held that discharging the takings claims would violate the Fifth Amendment's Takings Clause—and, more specifically, its prohibition on taking property without just compensation[17] incorporated against the states via

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7 *See In re City of Detroit*, 524 B.R. at 160.

8 *Id.* at 262.

9 *See, e.g.*, Objections of Creditors Deborah Ryan, Walter Swift, Cristobal Mendoza and Annica Cuppetelli, Interested Parties, to Amended Plan for the Adjustment of Debts of the City of Detroit at 2–3, *In re City of Detroit*, 524 B.R. 147 (Bankr. E.D. Mich. 2014) (No. 13-53846) (making claims under the Civil Rights Act of 1871, 42 U.S.C. §§ 1983 and 1985, and 28 U.S.C. § 1343).

10 *Id.*

11 U.S. CONST. amend. V.

12 *See generally* Joint Objection to Chapter 9 Plan by Creditors T&T Management, Inc., HRT Enterprises, and the John W. and Vivian M. Denis Trust Regarding the Treatment of Claims for Taking of Private Property Without Just Compensation, *In re City of Detroit*, 524 B.R. 147 (Bankr. E.D. Mich. 2014) (No. 13-53846).

13 *Id.*

14 *See In re City of Detroit*, 524 B.R. at 262; *see also infra* Part I.A (defining a "discharge").

15 *In re City of Detroit*, 524 B.R. at 262.

16 *Id.*

17 *Id.* at 268.

the Fourteenth Amendment.[18] The court addressed these constitutional concerns by modifying the plan to make takings claims immune from any discharge.[19]

This leads to the question at the heart of this Comment: Does the Takings Clause create special constitutional protections that prevent takings claims from being discharged in municipal bankruptcy? Since *In re City of Detroit*,[20] a circuit split has emerged over this question.[21] On one side, the Ninth Circuit held that takings claims can be discharged in municipal bankruptcy.[22] It largely ignored the question's complexity, relying on the fact that § 1983 claims frequently are discharged without even considering whether the unique features of the Takings Clause make this analogy flimsy.[23] On the other side, the First Circuit explicitly rejected the Ninth Circuit's analysis.[24] It instead held that takings claims receive special constitutional protection against discharge.[25] The most immediate reason to care about this question is the direct financial consequences. While *In re City of Detroit*[26] and *In re City of Stockton*[27] involved relatively modest claims,[28] the First Circuit's holding in *In re Financial Oversight &*

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18 *See* Chi., Burlington & Quincy R.R. v. City of Chicago, 166 U.S. 226, 241 (1897) (noting the incorporation of the Takings Clause against the states).

19 *In re City of Detroit*, 524 B.R. at 270. While one can argue that "just compensation" is contextual and changes when a municipality is insolvent to accommodate discharge in municipal bankruptcy, courts have been skeptical of this approach. *See, e.g.*, Monongahela Nav. Co. v. United States, 148 U.S. 312, 326 (1893) (understanding the just compensation requirement rigidly). Still, an analogous argument in the emergency exception in takings law leaves room for this argument. *Cf.* Nestor M. Davidson, *Nationalization and Necessity: Takings and a Doctrine of Economic Emergency*, 3 BRIGHAM-KANNER PROP. RTS. CONF. J. 187, 202 (2014).

20 524 B.R. 147 (Bankr. E.D. Mich. 2014).

21 *Compare* Cobb v. Stockton (*In re City of Stockton*) 909 F.3d 1256, 1268 (9th Cir. 2018), *with In re* Fin. Oversight & Mgmt. Bd. (*In re Fin. Oversight & Mgmt. Bd. I*), 41 F.4th 29, 45 (1st Cir. 2022), *cert. denied sub nom.* Fin. Oversight & Mgmt. Bd. for Puerto Rico v. Coop. de Ahorro y Credito Abraham Rosa, 143 S. Ct. 774 (2023).

22 *In re City of Stockton*, 909 F.3d at 1266 ("The Takings Clause is only implicated in bankruptcy if the creditor has actual property rights. In other words, the creditor must have an '*in rem* right under nonbankruptcy law to look to specific items of property' in order for the debt to be paid ahead of unsecured creditors." (quoting 4 COLLIER ON BANKRUPTCY ¶ 506.03 (Alan N. Resnick & Henry J. Sommer eds., 16th ed. 2017))).

23 *Id.* at 1268.

24 *In re Fin. Oversight & Mgmt. Bd. I*, 41 F.4th at 41, 45.

25 *Id.*

26 *See* Joint Objection to Chapter 9, *supra* note 12, at 3–4, *In re City of Detroit*, 524 B.R. 147 (Bankr. E.D. Mich. 2014) (No. 13-53846) (noting one takings creditor was entitled to $3,800 a month).

27 909 F.3d 1256 (9th Cir. 2018).

28 *Id.* at 1262 (describing the $4,200,997.26 takings claim involved in the case).

Management Board[29] cost "Puerto Rico more than $300 million that otherwise could [have] be[en] used to provide much-needed public services and to support the Commonwealth's fiscal recovery" by immunizing takings claims from discharge.[30] Within Puerto Rico, the First Circuit's decision also applied to "[t]akings claims totaling tens of millions of dollars" against various government departments.[31] As Puerto Rico continues to rebuild its infrastructure in the wake of devastating hurricanes, every dollar counts.[32]

Yet possibly even more critical than these bottom-line numbers are the broader legal consequences that follow from how this question is resolved. For example, immunizing takings claims from discharge threatens to amplify litigation over what classifies as a takings claim and create thorny—if not intractable—problems about how to treat settlements over takings disputes. Perhaps most importantly, immunizing takings claims from discharge will often mean that municipal bankruptcy is no longer a viable option for cities in financial distress because of the quantity and magnitude of takings claims.[33] These problems will likely only be amplified by the Roberts Court's changes in takings jurisprudence that have introduced tremendous uncertainty about what constitutes a taking.[34]

Ultimately, the Comment concludes that takings claims are constitutionally dischargeable in municipal bankruptcy—and in

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29 41 F.4th 29 (1st Cir. 2022).

30 Petition for Writ of Certiorari at 2, Fin. Oversight & Mgmt. Bd. for Puerto Rico v. Coop. de Ahorro y Credito Abraham Rosa, 143 S. Ct. 774 (2023) (No. 22-367).

31 *Id.* at 23.

32 *See, e.g.*, *2023 Hurricane Fiona Recovery Overview*, FEMA (Dec. 20, 2023), https://perma.cc/7MMD-YZT2.

33 *See infra* Part IV.A (discussing these practical consequences).

34 *See, e.g.*, Cedar Point Nursery v. Hassid, 141 S. Ct. 2063, 2074 (2021) (holding that a state regulation giving union organizers a limited right to enter the property of agriculture employers constituted a "*per se* physical taking" violating "the Fifth and Fourteenth Amendments"); *see also* LINDA GREENHOUSE, JUSTICE ON THE BRINK: THE DEATH OF RUTH BADER GINSBURG, THE RISE OF AMY CONEY BARRETT, AND TWELVE MONTHS THAT TRANSFORMED THE SUPREME COURT 224 (2021) (describing *Cedar Point* as a "potentially transformational development in the law of property rights" that is "likely to hobble government land use regulation"); Aziz Z. Huq, *Property Against Legality: Takings After* Cedar Point, 109 VA. L. REV. 233, 237 (2023) ("[*Cedar Point*] changes, potentially quite dramatically, the scope of constitutional protection for real property under the Takings Clause of the Fifth Amendment."). *But see* Rebecca Hansen & Lior Jacob Strahilevitz, *Toward Principled Background Principles in Takings Law*, 10 TEX. A&M L. REV. 427, 432 (2023) (arguing that "[c]ritics' darkest fears of *Cedar Point* probably will not materialize, at least for laws that are already on the books[,]" because of statutes of limitations).

doing so provides the first explanation from first principles for the Ninth Circuit's position.[35] After showing that, as a formal matter, there is space in the Constitution for takings claims to be dischargeable, this Comment develops historical and normative arguments that show that takings claims indeed are dischargeable. This Comment shows that the Takings Clause was originally understood to have a two-tier structure that would strongly protect individual property rights in areas with a risk of process failure—where normal procedural and political safeguards could not be trusted to guard against abuse—and would otherwise mostly get out of the way.[36] Various institutional features of the municipal bankruptcy regime guard extensively against abuse, which means that the Takings Clause should be highly permissive in enabling takings claims to get discharged under this two-tier model.[37] Normatively, takings claims should be dischargeable because doing so brings considerable societal gain without causing problematic harm to takings creditors, given that they will rarely ever be harmed by the operation of municipal bankruptcy as a whole.[38]

The Comment proceeds as follows. Part I provides legal background by first more precisely defining the question explored by the Comment and then analyzing the circuit split. Part II shows that formalist arguments—advanced in detail by the First Circuit and in dissent in the Ninth Circuit—that takings claims cannot be dischargeable fail because they rely on questionable assumptions about the nature of the right to just compensation and the legal mechanics of discharge. Finally, Parts III and IV respectively present the historical and normative arguments for why takings claims should be dischargeable.

This Comment offers a path to do justice to the unique logic and history of the Takings Clause, while still allowing takings claims to function flexibly in contemporary society. The Takings Clause can be appropriately acknowledged without obstructing an important tool for revitalizing communities.

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[35] More precisely, this Comment argues that takings claims are dischargeable only when (1) takings creditors lack a property interest securing their takings claim and (2) the relevant takings occurred prior to the initiation of municipal bankruptcy. *See supra* Part I.A (describing these qualifications).

[36] *See, e.g.*, William Michael Treanor, *The Original Understanding of the Takings Clause and the Political Process*, 95 COLUM. L. REV. 782, 855 (1995); *infra* Part III.A.

[37] *See infra* Part III.B.

[38] *See infra* Part IV.

I. SETTING UP THE QUESTION: ARE TAKINGS CLAIMS CONSTITUTIONALLY DISCHARGEABLE?

Can municipalities constitutionally leverage the bankruptcy regime to get off the hook for paying the full value of takings claims owed to litigants? This question, first considered in *In re City of Detroit*, has since spiraled into a live circuit split about whether takings claims are constitutionally immunized from discharge in municipal bankruptcy. After providing some further background on the exact question disputed, this Part will discuss the diverging analyses of the two circuits.

A. Defining the Question

Before diving into the circuit split, it will be helpful to clarify the exact question in dispute. The Takings Clause prohibits the government from taking property without just compensation.[39] After a taking happens, litigants can bring takings claims to try recovering just compensation from the municipality. Can a municipality take advantage of the municipal bankruptcy regime set up by Congress and get its obligation to pay just compensation discharged—where, instead of having to pay the full value of the taken land, it must only pay pennies on the dollar? Stated more formally, this question is whether Congress, in using its constitutionally enumerated bankruptcy powers,[40] can authorize bankruptcy courts to discharge takings claims against municipalities. The rest of this Section will unpack the different components of this question and clarify some aspects of the question that will be outside the scope of the legal dispute and the Comment.

The first important matter to clarify is what this Comment means by takings claims. The specific takings claims at issue involve litigants seeking just compensation from a municipality as a remedy for taken property.[41] For the purposes of this Comment, it does not matter what the alleged taking underlying the takings claim is: it may involve either the government directly taking property or a regulatory taking, where a regulation restricts the

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

40 *Id.* art. I, § 8, cl. 4.

41 *See infra* Part I. Thus, takings claims asking for other kinds of remedies, like injunctive and declaratory relief, will be outside the scope of this Comment.

owner's rights to such an extent that it is classified as a taking.[42] Takings claims against municipalities are typically brought under § 1983[43] or state law.[44] The Comment will examine whether takings claims can be brought directly under the Constitution without relying on subconstitutional sources of law like federal statutes or state law.[45] Importantly, this Comment will focus only on unsecured takings claims. Unlike secured takings claims, unsecured takings claims are not accompanied by a property interest functioning as collateral to underwrite the claim.[46] There are some added legal wrinkles in determining whether the Takings Clause protects secured takings claims from being discharged, which this Comment will briefly discuss. But the Bankruptcy Code already protects secured claims from discharge, so there is little practical urgency in determining whether they are constitutionally dischargeable.[47]

The next important dimension of the question to clarify is what it means for takings claims to be discharged. Formally, a discharge operates as a form of injunctive relief granted by the bankruptcy court that limits what the litigant can recover via existing (and future) judgments against the municipality.[48] To clear up a potential confusion, the discharge affects the ability of the takings creditor to recover just compensation only from the municipality in bankruptcy; nothing in the discharge prevents the

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[42] *See* Dave Owen, *The Realities of Takings Litigation*, 47 BYU L. REV. 577, 586–87 (2022) (analyzing the distribution of direct and regulatory takings claims in federal court).

[43] *See* Monell v. N.Y. Dep't of Soc. Serv., 436 U.S. 658, 690–91 (1978) (recognizing that § 1983 creates a cause of action for litigants to recover damages from municipalities for constitutional violations, including takings without just compensation). *But see* Ann Woolhandler & Julia D. Mahoney, *Federal Courts and Takings Litigation*, 97 NOTRE DAME L. REV. 679, 712 (2022) (arguing that much federal takings litigation should instead arise under the federal-questions statute, 28 U.S.C. § 1331).

[44] *See, e.g.*, *In re City of Stockton*, 909 F.3d at 1269 (noting that the litigant brought his takings claim under state law).

[45] *See infra* Part II.A.

[46] *See* 4 COLLIER ON BANKRUPTCY ¶ 1.02 (Alan N. Resnick & Henry J. Sommer eds., 16th ed. 2017) [hereinafter 4 COLLIER ON BANKRUPTCY]; *infra* Part I.A (discussing this focus on unsecured takings claims).

[47] There is one more technical carveout: takings claims that arise in litigation only after a municipality has filed for bankruptcy are outside the scope of the Comment. This is because postfiling claims are generally ineligible for discharge under the municipal Bankruptcy Code. 4 COLLIER ON BANKRUPTCY, *supra* note 46, ¶ 1.02. There would be reasons to worry if a municipality in municipal bankruptcy could just go on a takings spree knowing it will not have to pay much back—but this is blocked by the Bankruptcy Code and may even raise constitutional problems.

[48] *See id.*

litigant from recovering just compensation for the takings from a different party. This Comment asks whether Congress can constitutionally make takings claims dischargeable. It assumes that the core features of municipal bankruptcy stay relatively fixed—including, in particular, the host of procedural safeguards within municipal bankruptcy that guard against the worst kinds of abuse.[49] Congress's constitutional authority to make takings claims dischargeable plausibly depends on the municipal bankruptcy regime it creates.

B. The Emerging Circuit Split

A circuit split has emerged over whether takings claims are constitutionally dischargeable in municipal bankruptcy. The Ninth Circuit held that takings claims are dischargeable, though in doing so it largely ignored the key constitutional question. The First Circuit sharply disagreed, holding that the Takings Clause constitutionally immunizes takings claims from discharge during municipal bankruptcy. The remainder of this Section will survey these two decisions, which set the stage for the Comment's arguments about how this circuit split should be resolved.

1. The Ninth Circuit.

Four years after *In re City of Detroit*, the Ninth Circuit faced this question of whether takings claims are dischargeable in the context of the municipal bankruptcy of Stockton, California.[50] At the time of its filing, Stockton became the largest city to file for bankruptcy after the "housing market crash left it unable to pay its workers, pensioners and bondholders."[51] The Ninth Circuit faced a challenge from a takings creditor, Michael Cobb, who objected to the bankruptcy court preparing to discharge his claim.[52] Cobb's takings claim derived from land that was taken through a "quick-take procedure."[53] Under quick-take procedures, the government takes possession of the property after "depositing a probable compensation amount determined by a qualified expert

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[49] *See infra* Part III.B.

[50] *See In re City of Stockton*, 909 F.3d at 1265–66.

[51] Jim Christie, *Stockton, California to File for Bankruptcy*, REUTERS (June 27, 2012), https://www.reuters.com/article/world/stockton-california-to-file-for-bankruptcy-idUSBRE85Q1S2/.

[52] *In re City of Stockton*, 909 F.3d at 1259.

[53] *Id.* at 1261.

appraiser."[54] If the owner withdraws the deposit, they waive all claims and defenses to the property, except for one: a takings claim for just compensation for the taken land, which they are entitled to bring under state law.[55] Cobb's claim derived from land that his father owned, which Stockton took in 1998 through a quick take to build a road.[56] After inheriting the taken land from his father, Cobb withdrew the money Stockton had deposited with the California State Treasurer—and in doing so, he waived all his interests in the land except for the remaining takings claim for just compensation.[57] He was in the process of litigating this takings claim when Stockton began its bankruptcy proceedings.[58] Once bankruptcy began, Cobb objected to his claim being discharged.[59] The bankruptcy judge overruled Cobb's objection, explaining that if Cobb recovered a judgment, it would simply be a general unsecured debt amenable to discharge.[60] Cobb challenged that ruling, and the case went to the Ninth Circuit.[61]

Although the Ninth Circuit relied primarily on the doctrine of equitable mootness—dismissing Cobb's appeal because he did not seek a stay of the plan before it was authorized by the bankruptcy court and lacked an adequate reason for this delay[62]—it rejected Cobb's constitutional challenge on the merits.[63] On the Ninth Circuit's theory, "[t]he Takings Clause is only implicated in bankruptcy if the creditor has actual property rights."[64] The creditor must have an "*in rem* right under nonbankruptcy law to look to specific items of property" to underwrite their takings claim in order for the claim to be protected from discharge.[65] In other words, the Takings Clause prevents discharge only of *secured* takings claims, which are those backed up by a property interest that functions as collateral for the claim. The Ninth Circuit then found

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54 *See id*.

55 *See id*. at 1277 (Friedland, J., dissenting).

56 *Id.* at 1260 (majority opinion).

57 *In re City of Stockton*, 909 F.3d at 1261.

58 *Id.* at 1261–62.

59 *Id.* at 1262.

60 *See id*.

61 *Id.* at 1263.

62 *In re City of Stockton*, 909 F.3d at 1266. This doctrine of equitable mootness is designed to give finality to an approved bankruptcy plan. *Id.* at 1263.

63 *Id.* at 1269.

64 *Id.* at 1266.

65 *Id.* (quoting 4 COLLIER ON BANKRUPTCY, *supra* note 46, ¶ 506.03).

it clear that Cobb's claim was unsecured and thus dischargeable.[66] Cobb's takings claim was unsecured because he waived any property rights in the taken parcel securing his claim in two independent ways: by (1) withdrawing the quick-draw deposit and (2) allowing the City to construct the road and open it to public use.[67]

While Cobb's claim is relatively easy to classify as unsecured, and thus dischargeable under the Ninth Circuit's test, there will be harder cases. For example, when the takings creditor never officially waives their ownership interest in the taken property, it will be harder to determine if their claim is secured. Although neither courts nor scholarship give any detailed framework for determining the security status of takings claims, such status will ultimately turn on state property law and whether it recognizes a property interest backing up the takings claim as collateral.[68] The Ninth Circuit justified its test—where takings claims are dischargeable if they are unsecured—by focusing on when discharging a takings claim itself constituted a taking of property under the Takings Clause.[69] When a secured takings claim is discharged, the property interest securing the claim is itself taken through the discharge, which raises Takings Clause issues (at least on some theories).[70]

But no taking occurs when unsecured takings claims are discharged. The only thing an unsecured takings creditor loses when their claim is discharged is their right to recover a certain amount of money, which is not taken property for the purposes of the Takings Clause.[71] Indeed, the position that discharging unsecured takings claims is not itself a taking is supported by Supreme Court precedent.[72] The other side of the circuit split even seems

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66 *In re City of Stockton*, 909 F.3d at 1266.

67 *Id.* at 1266–67.

68 Of course, federal law in general, and the Constitution in particular, may set constraints on when state law can recognize a security interest backing up a takings claim.

69 *In re City of Stockton*, 909 F.3d at 1266 (citing 4 COLLIER ON BANKRUPTCY, *supra* note 46, ¶ 506.03).

70 *See, e.g.*, Julia Patterson Forrester, *Bankruptcy Takings*, 51 FLA. L. REV. 851, 870–80 (1999) (discussing how discharging secured claims can count as an unconstitutional taking). *But see* 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, 974 (1983) (arguing that discharging secured claims does not generally count as a taking).

71 *See In re City of Stockton*, 909 F.3d at 1267.

72 *See* Louisville Joint Stock Land Bank v. Radford, 295 U.S. 555, 589–90 (1935) (drawing a distinction based on whether the bankruptcy discharge deprives the owner "of substantive rights in specific property," like a lien); United States v. Gen. Motors Corp.,

to concede the point.[73] Yet even after granting this point, as the Comment does going forward, another question remains: Do unsecured takings claims receive constitutional protection because they arise out of the Takings Clause? The Ninth Circuit relied on an analogy to quickly dismiss the possibility that unsecured takings claims receive protections from their constitutional pedigree.[74] It found that because "other constitutionally based lawsuits seeking money damages, such as § 1983 claims, are routinely adjusted in bankruptcy," there is no reason to treat unsecured takings claims differently because of their constitutional status.[75] Conspicuously, the Ninth Circuit made no effort to engage with the counterargument, raised in Judge Michelle Friedland's dissent, that there are considerable disanalogies between takings claims and other damages claims for constitutional violations.[76]

Judge Friedland's dissent criticized the majority's cursory answer to this question about unsecured takings claims.[77] In stark contrast to the majority, Judge Friedland's analysis reached the conclusion that "as a matter of constitutional first principles, . . . municipalities are obligated to provide just compensation for any taking of private property, regardless of the bankruptcy laws."[78] Although Judge Friedland could not ground this conclusion in a perfectly analogous Supreme Court case, she pointed to Supreme Court "decisions underscor[ing] that Congress's bankruptcy powers do not allow it to infringe upon rights guaranteed by the Takings Clause."[79] Judge Friedland's dissent argued that Cobb's takings claim should have special protection in bankruptcy, even if unsecured, because "the Takings Clause stands

323 U.S. 373, 378 (1945) (defining "property" for the purposes of the Takings Clause as "the group of rights inhering in the citizen's relation to the physical thing, as the right to possess, use and dispose of it"). Because unsecured takings creditors have a right only to recover compensation and do not have a right to possess, use, or dispose of the now-taken physical property, the discharge of takings claims will not itself count as a taking of property under *Radford* or *General Motors*.

73 *See In re City of Detroit*, 524 B.R. at 270 ("The taken property here is not the creditor's unsecured claim in bankruptcy."); *In re Fin. Oversight & Mgmt. Bd. I*, 41 F.4th at 43 ("[T]he relevant question is whether denial of just compensation for [a taking prior to bankruptcy] violates the Fifth Amendment.").

74 *In re City of Stockton*, 909 F.3d at 1268.

75 *Id.*

76 *See id.* at 1279–80 (Friedland, J., dissenting).

77 *See id.* at 1269.

78 *Id.* at 1271.

79 *In re City of Stockton*, 909 F.3d at 1273 (Friedland, J., dissenting).

alone among constitutional provisions in requiring a specific compensatory remedy."[80] Because Cobb "has a constitutional right *to just compensation*," bankruptcy discharge directly infringes on that constitutional right.[81] While Judge Friedland conceded that § 1983 claims for other constitutional violations—like the civil rights claims in Detroit[82]—are frequently discharged, she argued that "nothing in the Constitution expressly guarantees compensation for" those constitutional violations.[83] This unique way in which takings claims are anchored in the Constitution justifies treating them differently from other constitutional claims, which rely on subconstitutional law to recover compensation in the wake of a constitutional violation. A main contribution of this Comment will be to fill the hole in the majority's opinion and develop a comprehensive response from first principles to Judge Friedland's critique.

2. The First Circuit.

The First Circuit faced the same question about the dischargeability of takings claims when Puerto Rico declared bankruptcy under Title III of the Puerto Rico Oversight, Management, and Economic Stability Act[84] (PROMESA).[85] After Puerto Rico's governor declared it unable to pay its debts in 2015,[86] Congress passed PROMESA and created the Puerto Rico Financial Oversight and Management Board to restructure Puerto Rico's liabilities (consisting of more than $72 billion in debt and $55 billion in pension liabilities).[87] The bankruptcy proceedings that followed involved a substantial number of takings creditors, including many like Cobb whose claims arose from quick-taking procedures.[88] An earlier plan would have discharged these claims significantly and only allowed takings creditors to recover "at a pro-rata share of the overall recovery for general unsecured creditors."[89] Predictably, takings creditors objected to the discharge of

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80 *Id.* at 1279.

81 *Id.* (emphasis in original).

82 *See supra* notes 15–19 and accompanying text.

83 *In re City of Stockton*, 909 F.3d at 1279.

84 48 U.S.C. § 2101 et seq.

85 *See In re Fin. Oversight & Mgmt. Bd. I*, 41 F.4th at 37.

86 David Skeel, *Reflections on Two Years of P.R.O.M.E.S.A.*, 87 REVISTA JURICADA UNIVERSIDAD DE P.R. 862, 862 (2018).

87 Lorae Stojanovic & David Wessel, *Puerto Rico's Bankruptcy: Where Do Things Stand Today?*, BROOKINGS INST. (Aug. 17, 2022), https://perma.cc/RW5C-T7Z3.

88 *In re Fin. Oversight & Mgmt. Bd. I*, 41 F.4th at 38.

89 *Id.*

their claims on the same constitutional grounds raised in *In re City of Detroit* and *In re City of Stockton*.[90] The court managing Puerto Rico's bankruptcy pursuant to PROMESA agreed with these objections and directed the Board to modify the plan to immunize takings claims from discharge.[91] An appeal to the First Circuit followed.[92]

The First Circuit's analysis began with the premise that "bankruptcy laws are subordinate to the Takings Clause."[93] Thus, what ultimately matters is whether the Takings Clause allows takings claims to be discharged. The court considered the Board's first argument—familiar from *In re City of Stockton*—that the Takings Clause only prohibits discharging secured takings claims.[94] The court rejected this argument fairly quickly for lacking an appropriate basis in case law.[95] As noted earlier, this conclusion is quite plausible: even if the discharge of takings claims is not itself a taking, such discharge might run afoul of the Takings Clause by impeding the takings creditor's constitutional right to just compensation from the original taking.

Similarly, the court rejected the Board's second argument that takings claims should be dischargeable because they are similar to other damages claims for constitutional violations, which are routinely discharged without constitutional issues.[96] Here, the First Circuit explicitly rejected the argument embraced by the Ninth Circuit.[97] On the First Circuit's reading, "[t]he language and nature of the Takings Clause [ ] suggests . . . that just compensation is different in kind from other monetary remedies."[98] The just compensation requirement is more than "a remedy for a constitutional wrong"; it is also a "structural limitation on the government's very authority to take private property."[99] In this sense, the right to just compensation follows directly from the Constitution given that "the Fifth Amendment contemplates a 'constitutional obligation to pay just compensation,'" whereas other claims for damages arising from a constitutional violation "lack an

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90 *Id.* Notably, they did not raise the argument that their claims were secured. *See id.*

91 *Id.* at 39.

92 *In re Fin. Oversight & Mgmt. Bd. I*, 41 F.4th at 39.

93 *Id.* at 42.

94 *Id.*

95 *Id.* at 44.

96 *Id.*

97 *See supra* note 74.

98 *In re Fin. Oversight & Mgmt. Bd. I*, 41 F.4th at 44.

99 *Id.*

express basis in the Constitution."[100] The court also focused on the fact that the Takings Clause specifies "both a monetary remedy and even the necessary quantum of compensation due."[101] All this should sound familiar from Judge Friedland's dissent.

After responding to the Board's arguments, the court concluded that takings claims are immunized from discharge on "rather simple" grounds: the Takings Clause "provides that if the government takes private property, it must pay just compensation," so bankruptcy proceedings cannot diminish this constitutional "obligation by the Commonwealth to pay just compensation."[102] Thus, on the First Circuit's understanding, the Constitution as a formal matter gives special protection to takings claims. Because the right to recover just compensation in the wake of a taking is uniquely anchored in the Constitution, a bankruptcy judge cannot interfere with that right by issuing a discharge.

II. THE LIMITS OF FORMALISM FOR ANSWERING THE QUESTION

Both the *In re Financial Oversight & Management Board* and *In re City of Detroit* courts ultimately relied on simple formalist considerations, which can be fairly characterized by the following argument. The Constitution directly creates a right to recover just compensation for a taking, and discharging takings claims would deprive takings creditors of that constitutional right. Therefore, discharging takings claims is unconstitutional. This argument seems quite plausible on its face. If the Constitution directly gives individuals a right to recover just compensation in the wake of a taking, Congress should not be able to empower bankruptcy judges to issue injunctions preventing individuals from exercising their constitutional right to recover just compensation. But the argument's persuasive force rests on two masked assumptions.

The first assumption concerns what kind of right to just compensation the Constitution creates. Even if the Constitution directly creates a right to just compensation for taken property, it may not directly create a right to recover just compensation *from the municipality*. Given the complex nature of state governments, it is more plausible that the Constitution does not take a stance on whether it is the municipality or, for example, the state as a

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[100] *Id.* at 44–45 (quoting First Eng. Evangelical Lutheran Church v. County of Los Angeles, 482 U.S. 304, 314 (1987)).

[101] *Id.* at 45.

[102] *Id.* at 46.

whole that has the responsibility to pay just compensation.[103] It thus takes a federal statute or state law to fill in this gap and force municipalities to pick up the bill. The important point is that when takings creditors have claims for just compensation from a municipality, their claims very plausibly depend on subconstitutional law and thus can be discharged without constitutional problems in the same way § 1983 claims for constitutional violations are often and uncontroversially discharged.[104] Even though as a practical matter the municipality may be the only plausible target for just compensation, this is a contingent feature of subconstitutional law and does not mean the municipality has an obligation to pay that is constitutional in nature (and thus immunized from discharge).

The second assumption concerns how to characterize the way bankruptcy courts discharge a takings claim. One natural characterization is that discharge involves an external legal force trying to shrink the right created by the Takings Clause. Here, the discharge impinges on what takings creditors are constitutionally entitled to. This raises an obvious legal problem: because bankruptcy judges only have authority from statutes and the Constitution trumps statutes, bankruptcy judges are powerless to issue a discharge that conflicts with the constitutional right to just compensation.

But an alternative characterization of discharge avoids this problem and shows how a constitutional right can be discharged without requiring bankruptcy judges to transgress the Constitution. On this second characterization, the right to just compensation is dischargeable by the very nature of the legal interest created by the Takings Clause. Much like how some property interests are set up to terminate under certain conditions,[105] the right to recover just compensation may be set up to shrink when it is discharged in bankruptcy. If the right to just compensation has this internal dischargeability—where the legal interest has built into it the limitation that it shrinks when certain

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[103] Or perhaps the Constitution simply directs the obligation to pay just compensation to the state as a whole.

[104] *See In re City of Detroit*, 524 B.R. at 265 (describing why the claims of civil rights creditors with § 1983 claims against the City could be discharged); *In re City of Stockton*, 909 F.3d at 1268 (noting that § 1983 claims to vindicate constitutional rights are "routinely adjusted").

[105] *See infra* note 142 and accompanying text (giving an example of property held as a fee simple determinable).

conditions are triggered—the constitutional right can be discharged without any violation of the Constitution.

While this Part does not argue that this second characterization is more fitting than the first, the point is that this second characterization is another possibility. It thus is a mistake to think that the discharge of a constitutional right means a constitutional right is being violated. One would first need to know what kind of discharge is occurring. This provides another escape hatch from the argument that takings claims, as a formal matter, *must* be protected from discharge. While the earlier assumption focused on the constitutional status of the right to just compensation from a municipality, this second assumption is about the content of the right. Even if the right to recover just compensation from a municipality is constitutional, it still may be dischargeable if dischargeability is built into the right.

This Part will explore these two assumptions in depth, showing that simple formalist arguments do not require takings claims to be immunized from discharge. Importantly, unmasking these two assumptions offers two independent ways to resist the formalist argument. As long as at least one of these responses is viable, the stage is set for the historical and normative considerations that will make up the rest of the Comment.

A. Two Rights to Just Compensation

The formalist argument in favor of immunizing takings claims from discharge depends on the idea that takings creditors have a right to recover just compensation that is directly in the Constitution.[106] But this argument only works if the difference between two rights to just compensation is obscured. To start, there is the takings creditor's general right to receive just compensation in the wake of a taking. The Supreme Court recently noted that it was an open question whether the Takings Clause (together with the Fourteenth Amendment) directly creates a cause of action to recover just compensation after a taking.[107] Yet even if it

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[106] *See In re City of Detroit*, 524 B.R. at 265 (noting that unlike the Takings Clause, "the Fourteenth Amendment does not provide a substantive constitutional right to compensation for damages"); *In re City of Stockton*, 909 F.3d at 1279 (Friedland, J., dissenting); *In re Fin. Oversight & Mgmt. Bd. I*, 41 F.4th at 44–45.

[107] *See* DeVillier v. Texas, 144 S. Ct. 938, 944 (2024) ("Our precedents do not cleanly answer the question whether a plaintiff has a cause of action arising directly under the Takings Clause. But this case does not require us to resolve that question.").

is assumed for the sake of argument that the Constitution directly creates a general right to recover just compensation after a taking,[108] this general right is not what gets impaired in discharge. Instead, what is impaired is the more specific right to recover just compensation *from the municipality*.[109] A bankruptcy court's discharge, after all, affects the ability of the takings claimant to recover judgments only against the municipality and leaves the rest of the world untouched as potential targets for recovery.[110]

While there is a right to recover just compensation from municipalities, this specific right almost certainly derives from federal statute[111] and state law and thus can be discharged without any constitutional problems.[112] In other words, while the Constitution may directly create a general right to recover just compensation after a taking, it is unlikely that the Constitution directly creates a specific right to recover just compensation from the municipality—and only this second right gets impinged by municipal bankruptcy.

The absence of a direct constitutional right to recover just compensation from a municipality is first suggested by the text of the relevant constitutional provisions, namely the Takings Clause and the Fourteenth Amendment. First, consider the text of the Takings Clause: "[N]or shall private property be taken for public use, without just compensation."[113] It is written exclusively as a prohibition—describing conditions under which the government cannot take property—and leaves open what exactly happens if the government violates the Takings Clause and

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[108] *See First Eng.*, 482 U.S. at 315 (suggesting this understanding of the Takings Clause as a consequence of its "self-executing character," though the opinion is amenable to other interpretations). Indeed, the Supreme Court rejected this interpretation of *First English* and found it to be an open question whether the Takings Clause ever creates a cause of action for recovery. *DeVillier*, 144 S. Ct. at 943–44.

[109] *See, e.g.*, *In re City of Detroit*, 524 B.R. at 267 (describing how the discharge involved takings claims, either already litigated or in litigation, specifically against Detroit).

[110] *See supra* notes 48–49 and accompanying text.

[111] *See, e.g.*, Aditya Bamzai & David N. Goldman, *The Takings Clause, the Tucker Act, and* Knick v. Township of Scott, YALE J. ON REGUL.: NOTICE & COMMENT (Oct. 9, 2018), https://perma.cc/CBA2-HKLK (describing how "the scheme for remedying takings claims against . . . municipal governments can be found in . . . § 1983").

[112] *Cf.* Christopher Serkin, *Big Differences for Small Governments: Local Governments and the Takings Clause*, 81 N.Y.U. L. REV. 1624, 1661–64 (2006) (arguing that the Takings Clause ought to apply differently to local governments based on political-economic considerations); Mark D. Rosen, *The Surprisingly Strong Case for Tailoring Constitutional Principles*, 153 U. PA. L. REV. 1513, 1571 (2005) (noting that states and municipalities "might be sufficiently different to justify differential treatment as a constitutional matter").

[113] U.S. CONST. amend. V.

unconstitutionally takes property.[114] The text does not explicitly describe a remedial scheme where, in the event of an unconstitutional taking, a particular government entity has an obligation to pay just compensation.

Second, consider the text of the Due Process Clause of the Fourteenth Amendment, which incorporates the Takings Clause against the states: "[N]or shall any State deprive any person of life, liberty, or property, without due process of law."[115] This language focuses on the state as a whole. It is hard to read into the language a specific stance on whether the state as a whole or some specific political subdivision bears the responsibility to pay just compensation after a taking. Indeed, the Fourteenth Amendment's Enforcement Clause[116] plausibly empowers Congress[117] to settle these details about how a constitutional requirement to pay just compensation should be grafted onto varied and complex state governmental institutions.[118] In short, from the perspective of the constitutional text, the municipality is nowhere to be found. While these considerations by themselves would only be decisive for the strictest textualist, they give an initial reason to doubt whether the Constitution singles out the municipality as the entity responsible for paying just compensation.

This absence of a direct constitutional right to recover just compensation from a municipality is further suggested by the history of local governments. Throughout the early eighteenth century, the very structure of American local government law began remarkably haphazardly as a "transition from the English law of corporate boroughs to the American law of municipal corporations," which varied across different states.[119] Indeed, the

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114 *Cf. id.* amend. IV (prohibiting certain "unreasonable searches and seizures" but not explicitly providing for any specific remedy in the event an unconstitutional search or seizure occurs).

115 *Id.* amend. XIV, § 1.

116 *Id.* amend. XIV, § 5.

117 *But see* City of Boerne v. Flores, 521 U.S. 507, 519–20 (1997) (identifying limits to Congress's powers under the Enforcement Clause).

118 *See also* Devillier v. Texas, 63 F.4th 416, 421–22 (5th Cir. 2023) (en banc) (Higginson, J., concurring in denial of rehearing) (noting that even if the Takings Clause creates a cause of action to recover just compensation from the federal government, there are considerable questions about how and whether that cause of action is incorporated against the states).

119 Joan C. Williams, *The Invention of the Municipal Corporation: A Case Study in Legal Change*, 34 AM. U. L. REV. 369, 372 (1985); *see also* Hendrik Hartog, *Because All the World Was Not New York City: Governance, Property Rights, and the State in the Changing Definition of a Corporation, 1730–1860*, 28 BUFF. L. REV. 91, 96–98 (1978).

Reconstruction Congress that proposed the Fourteenth Amendment was particularly familiar with the various legal structures of local government as they "sought to remake the very fabric of southern local government by imposing the model of the New England town through the new state constitutions."[120] With all this complexity and change in how state governments were structured, it is doubtful that the Constitution directly identifies some specific political subdivision of the state as responsible for paying just compensation.[121] It is more plausible that the Constitution leaves open who must pay the bill for a takings violation, or instead directs that obligation to the state as a whole.

The history of takings claim litigation in federal court confirms this position. Before the passage of § 1983, federal courts did not recognize a general right to recover just compensation from municipalities after a taking.[122] Instead, the Takings Clause functioned to invalidate government ownership when it attempted a taking without just compensation, which would justify enjoining the government from the property or awarding damages for trespass based on ordinary property law principles.[123] This history is not specific to takings claims against local government but speaks more generally to the logical structure of how takings claims were understood: the Takings Clause served as an ex ante limitation on when the government could acquire property, rather than as an ex post right to recover just compensation after the taking.[124] Still, this history adds doubt to the claim that the Constitution directly creates a right to recover just compensation from a municipality after a taking. Given that federal courts did not recognize a general right to recover just compensation through courts in the wake of a taking until well after § 1983

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120 Daniel Farbman, *Reconstructing Local Government*, 70 VAND. L. REV. 413, 417–18 (2017).

121 *See* Monell v. N.Y. Dep't of Soc. Serv., 436 U.S. 658, 686–87 (1978) (noting that one of the motivating factors for the drafters of the Civil Rights Act of 1871 was to create a mechanism for litigants to be able to recover damages from municipalities for takings, which suggests that the Fifth and Fourteenth Amendments were not understood as automatically granting a right to recover just compensation from municipalities).

122 *See* Woolhandler & Mahoney, *supra* note 43, at 683–86 (noting that pre-§ 1983 takings cases tended to rely on diversity of citizenship).

123 *See id.*

124 *See* Knick v. Twp. of Scott, 139 S. Ct. 2162, 2176 (2019) (noting that "[a]ntebellum courts . . . had no way to redress the violation of an owner's Fifth Amendment rights other than ordering the government to give [them] back [their] property").

became law, there is reason to doubt that the Constitution itself directly created that right.

But perhaps it makes intuitive sense for the obligation to pay just compensation to be directed to whichever political subdivision is most directly responsible for the taking. This suggestion, however, runs into two fundamental problems. First, it is far from obvious that the municipality should have to pay just compensation given that centralized state governments often possess remarkable control over "local fiscal matters" and thus seem to be much better positioned to provide payment.[125] Second, given conventional doctrine about the legal status of local governments,[126] it is likely that states themselves are responsible for takings committed by local governments in the eyes of the Constitution. Under existing legal doctrine, the Constitution views local governments "as mere instrumentalities of their state governments rather than legally separate entities."[127] Thus, it is plausible that parent state governments, as opposed to municipal governments, are ultimately responsible for the taking—much like how many jurisdictions have laws that hold (literal) parents responsible for the wrongdoing of their children.[128] This possibility is especially credible given the practical realities of how much control centralized state governments exert on local governments.[129] Although litigants today face obstacles to recovering just compensation from the states,[130] this is a feature contingent on how Congress wrote and courts interpret § 1983, which says very little about the Constitution's perspective on who must pay the bill for takings. Indeed, the Supreme Court may remove these barriers by letting litigants bring takings claims against states directly under the Constitution.[131]

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125 *See* Felipe Ford Cole, *Unshackling Cities*, 90 U. CHI. L. REV. 1365, 1415 (2023).

126 *See id*. at 1413.

127 *See* Kathleen S. Morris, *The Case for Local Constitutional Enforcement*, 47 HARV. C.R.-C.L. L. REV. 1, 2–3 (2012) (describing the current mainstream view before challenging its merit); *see also* Atkin v. Kansas, 191 U.S. 207, 220 (1903) (noting that "[municipal] corporations are the creatures—mere political subdivisions—of the State").

128 *See, e.g.*, Sarah Swan, *Home Rules*, 64 DUKE L.J. 823, 838–44 (2015) (describing the rise of parental liability ordinances); Amy L. Tomaszewski, Note, *From Columbine to Kazaa: Parental Liability in A New World*, 2005 U. ILL. L. REV. 573, 576–80 (describing other forms of parental liability).

129 *See* Cole, *supra* note 125, at 1414–15.

130 *See* Ilya Somin & Isaiah McKinney, *The Fifth Amendment Is Self-Executing*, CATO INST. (May 17, 2023), https://perma.cc/U7MH-ZNMD.

131 *See DeVillier*, 144 S. Ct. at 944 (leaving open the question about whether the Takings Clause directly creates a cause of action to recover just compensation from a

Still, one might think that the distinction between the general right to recover just compensation and the specific right to recover just compensation from the municipality collapses because states are protected by common law sovereign immunity and the Eleventh Amendment.[132] In other words, the difference in theory between the general and specific rights falls apart in reality because the municipality is the only available target to sue for just compensation given that it is impossible to sue the state.

There are two reasons to reject this argument. First, neither sovereign immunity nor the Eleventh Amendment would make it *impossible* to recover just compensation from the state after recovery from the municipality is blocked by a discharge. One scholar has argued in depth that the Takings Clause automatically abrogates the common law sovereign immunity doctrine protecting states against suits;[133] even if that argument fails, states can always waive their common law immunity.[134] The Eleventh Amendment's immunity for states, while not waivable, only poses a bar to certain federal suits and leaves completely unimpaired suits to recover just compensation from states in *state* courts.[135] Second, even if the state is somehow shielded from suits for just compensation, there are other potential targets besides the municipality. One option would be to bring suits against state officials (who are not similarly immunized from suits), which remains an option today[136] and historically was the primary legal mechanism for accessing constitutional remedies.[137] Another option would be suing an intermediate political entity (between the municipality and the state), like a county, if the state government

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state). Of course, it is possible that the Supreme Court finds that the Takings Clause does not create a cause of action to recover just compensation from a state—but that effectively repudiates the position that takings claims against municipalities derive directly from the Constitution without depending on subconstitutional law. While it is theoretically possible that the Takings Clause directly creates a constitutional right to recover against municipalities but not against states, that is a very strange position. *See infra* notes 161–68 and accompanying text.

132 *See* William Baude, *Sovereign Immunity and the Constitutional Text*, 103 VA. L. REV. 1, 4–9 (2017) (describing different ways to understand sovereign immunity and its relationship to the Eleventh Amendment).

133 *See* Eric Berger, *The Collision of the Takings and State Sovereign Immunity Doctrines*, 63 WASH. & LEE L. REV. 493, 498–99 (2006).

134 *See* Baude, *supra* note 132, at 4.

135 *Id.* at 2.

136 *See id.* at 4.

137 *See* Richard H. Fallon, Jr., *Constitutional Remedies: In One Era and Out the Other*, 136 HARV. L. REV. 1300, 1313 (2023).

structure allows.[138] These two responses may seem hyperformalist: they point out that there are other routes to recover just compensation, even if as a practical matter they are hard to access. But the formalism should not be a problem here. This Part, after all, is only trying to respond to the argument that the Constitution—based on its formal structure—must immunize takings claims from discharge to keep the right to just compensation open. Therefore, showing that discharge does not foreclose all theoretical routes to recover just compensation is enough to counter the argument.[139]

Of course, one may still be unconvinced and think that as a formal matter there must be some practically effective way to vindicate the constitutional right to just compensation and, at least for now, the only realistic target is the municipality. To this, the most direct response is that the more one thinks the Takings Clause directly creates a right to just compensation, the more one should think that the Takings Clause pierces common law sovereign immunity and enables litigants to directly recover just compensation from the state in state court.[140] More generally, if the Constitution requires that there be some practical way for a takings creditor to recover just compensation, courts can fulfill this requirement by creating paths for takings creditors to recover from other sources after a discharge blocks recovery from the municipality. There may be policy reasons to prefer the status quo where the municipality is generally left paying the bill, but the Constitution itself does not dictate this institutional arrangement.

In summary, the simple formalist argument for immunizing takings claims from discharge fails because it confuses the general right to just compensation and the specific right to just compensation from the municipality. While the former might derive directly from the Constitution, the latter almost certainly does

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[138] *See, e.g.*, Tyler v. Hennepin County, 143 S. Ct. 1369, 1373 (2023) (involving a takings claim against a county).

[139] There may be another, less satisfying response. It is not obvious that a constitutional right to recover just compensation needs to be enforceable by courts. As one scholar has put it, the position that constitutional rights by their very nature include a "constitutionally mandated right to" effective judicial remedies "confronts gathering precedent-based headwinds." *See* Fallon, *supra* note 137, at 1306–07. Despite maxims to the contrary, rights very often come without remedies. Perhaps that is true of the right to just compensation.

[140] *See generally* Berger, *supra* note 133 (arguing at length that the Takings Clause automatically abrogates sovereign immunity).

not—and instead relies heavily on § 1983 and other subconstitutional legal provisions that force the municipality to pick up the bill to pay just compensation. Thus, when takings claims against the municipality are discharged, the discharge likely modifies a subconstitutional remedial scheme without direct constitutional protection, paralleling the way § 1983 claims for constitutional violations are frequently and uncontroversially discharged.[141] Although there certainly is room to resist these conclusions and argue that there is a link connecting the general right to recover just compensation to the specific right to recover just compensation from the municipality, it should be clear that the existence of such a link is far from obvious. Once this is recognized, the formalist pressure for immunizing takings claims from discharge is significantly weakened.

B. Two Kinds of Discharge

The second assumption underlying the formalist argument against discharge concerns its second premise that discharging a takings claim impinges on the constitutional right to just compensation. It certainly is true that discharge limits what the takings creditor can recover from the municipality via their right to just compensation. But the formalist argument depends on the stronger premise that discharging a takings claim *legally conflicts* with the constitutional right to just compensation. In other words, the argument relies on the tacit premise that discharge creates an impermissible legal arrangement where the takings creditor is prevented by a bankruptcy judge from doing what the constitutional right expressly permits them to do, namely recover just compensation. But this Section will show that the premise that discharge conflicts with the Constitution is false. There are two distinct ways to categorize discharge—which this Comment will call "external" and "internal" discharge, respectively—based on what causes a right to shrink, and only discharges of the first kind would be constitutionally problematic. Only the former involves this conflict where a bankruptcy judge attempts to prevent individuals from doing what their constitutional right permits them to do.

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[141] *See supra* note 104.

The upshot is that this Section offers another route to resist the formalistic conclusion that takings claims cannot be dischargeable. Even if one assumes that the Constitution directly creates a right to recover just compensation from a municipality, discharging this right may be constitutionally permissible. In particular, the discharge may simply be the realization of some possibility internal to the constitutional right, where a kind of self-shrinking is activated, rather than an effort by a bankruptcy judge to transgress constitutional requirements. While this Section simply articulates that takings claims *may* be internally dischargeable, it offers another route to show that formalism alone does not settle the circuit split.

These two kinds of discharge can be introduced with an analogy to property law. Suppose *A* receives the following conveyance of Blackacre: to *A* so long as Chicago is solvent.[142] If Chicago were ever to become insolvent, *A*'s property interest in Blackacre would automatically terminate. Notice that this termination does not come from some external legal force that trumps *A*'s property interest. Instead, this termination comes from the property interest *itself*, which is set up to terminate when Chicago goes broke. Importantly, when *A*'s property interest self-destructs during Chicago's insolvency, there is no need for any external legal force to come along and trump *A*'s interest. By contrast, when Chicago is solvent, *A*'s interest can only be terminated through some external force that trumps it—like Chicago exercising its eminent domain powers to take over Blackacre.

This leads to an important point. What can one infer from the fact that *A*'s ownership was terminated? It may be that an external legal force extinguished *A*'s ownership, in which case there is a valid worry that the external force inappropriately impinged on *A*'s ownership—like Chicago impermissibly using its eminent domain powers to take over Blackacre. But another possibility is that *A*'s interest self-destructed based on how the interest was set up. The mere fact that *A*'s interest is terminated thus does not tell us whether something impinged it. To answer that question, one would first need to know what kind of termination occurred. Just as *A*'s property interest is set up to terminate in certain situations, a legal interest can similarly be set up to discharge in

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142 *See* JESSE DUKEMINIER, JAMES E. KRIER, GREGORY S. ALEXANDER, MICHAEL H. SCHILL & LIOR JACOB STRAHILEVITZ, PROPERTY 295 (10th ed. 2022) (describing the creation of fees simple determinable).

certain situations. Instead of self-destruction, this is self-shrinking. For example, *B* might have a right that initially allows them to recover $500 from *A*, but by its very nature, the right may be set up to shrink when certain conditions obtain (for example, *A* gets fired), after which it enables *B* to recover only $250. This is the possibility of internal discharge. Discharge of a right does not need to involve some external force interfering with it but instead can be the activation of this self-shrinking process. Here, dischargeability is built into the right, allowing it to be discharged on suitable occasions without anything violating or impinging on the right.

While it may be natural to think of discharge in external terms, like Chicago taking Blackacre from *A*, internal discharge offers another option. To give another analogy, external discharge is like entering a house by knocking down the door, while internal discharge is like turning the key and peacefully entering. In the same way that it is a mistake to infer that the door was torn down from the fact that someone entered the house, it is wrong to infer that the constitutional right was violated because the right was discharged. This points to a core problem with the simple formalist argument: it tries to conclude a constitutional violation occurred from the fact that the constitutional right to just compensation was discharged. In doing so, this argument ignores that there are different kinds of discharges just like there are different kinds of entrances.

These two kinds of discharge are at the center of the Supreme Court's debate in *Ogden v. Saunders*.[143] There, the Marshall Court considered whether the Contracts Clause[144] prevented New York from passing a bankruptcy statute that would allow individuals to be "absolved from all future contractual obligations" in certain contexts when they defaulted.[145] Chief Justice John Marshall, in his "only dissent on a constitutional question," found a conflict with the Contracts Clause because the statute's discharges impaired contractual obligations.[146] On Chief Justice Marshall's understanding, the bankruptcy statute attempting to effect a discharge "[did] not enter into [contracts], and become a part of the

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143 25 U.S. (12 Wheat.) 213 (1827).

144 U.S. CONST. art. I, § 10, cl. 1.

145 Clyde Ray, *John Marshall,* Ogden v. Saunders*, and the Character of Neo-Republican Liberty*, 5 CONST. STUD. 31, 33 (2019).

146 *Id.* at 32.

agreement[s]," but instead functioned as an external attempt to "repeal or modify" contractual rights.[147] Chief Justice Marshall thus understood the discharges in external terms. By contrast, Justice Bushrod Washington—with his position prevailing on the Court—understood the statute as forming "part of the contract," which made it "a solecism to say" that the contractual obligations were impaired when they were discharged.[148] On his understanding, the contractual obligations incorporated the bankruptcy statute within their terms and thus included the possibility of self-shrinking during specified conditions. Contractual obligations could then be discharged without creating a conflict between the contracts and state law because dischargeability was built into the contractual obligations. Regardless of who was right in *Ogden*, the main point is that the case demonstrates the two kinds of discharge: Chief Justice Marshall sees the discharges in the case in external terms, as breaking down the door and infringing upon contracts, while Justice Washington sees discharge in internal terms, as twisting a key and activating the contract's built-in dischargeability, which triggers self-shrinking without infringing on contractual rights.

If takings claims are only discharged internally, then the discharge does not conflict with the constitutional right to just compensation. On this hypothesis, when the government takes property, the Takings Clause gives the former owner a right to just compensation, with dischargeability in municipal bankruptcy built into that right. So even if the Constitution directly gives a right to recover just compensation from the municipality, this right may be internally dischargeable—in which case the discharge of takings claims would be the peaceful turning of a key, as opposed to forcibly knocking down a door. This would mean that discharging takings claims does not transgress the constitutional right to recover just compensation but instead activates self-shrinking.

Of course, nothing has been said to argue that this hypothesis is true. Indeed, one might be skeptical that the taking creditor's interest in just compensation is internally dischargeable given that takings creditors will not generally be alert to the possibility of discharge in municipal bankruptcy. But it is far from obvious

147 *Ogden*, 25 U.S. at 343 (Marshall, C.J., dissenting).
148 *Id.* at 259–60 (opinion of Washington, J.).

that notice is the controlling factor, and Parts III and IV offer historical and normative considerations in favor of viewing these discharges as internal. The important takeaway is that it is not obvious whether discharging a takings claim is more like knocking down a door or turning a key. Formal logic alone thus does not resolve whether discharging takings claims is at odds with the Constitution.

III. THE TWO-TIER TAKINGS CLAUSE MEETS MUNICIPAL BANKRUPTCY

The history of the Takings Clause—both in terms of the specific intent of its drafters and the legal antecedents that shaped how it would be understood—reveals that it was designed to have a two-tier structure to strike a compromise between republican deference to elected majorities and liberal concern with individual property. Generally, the Takings Clause would merely serve as an instructional tool, but it would activate to provide strong protections of property rights in areas where the political process faced a strong risk of malfunctioning.[149] Making takings claims dischargeable is a natural extension of this two-tier structure: elected majorities are allowed to move forward by restructuring the municipality's debts, while extensive procedural protections protect takings creditors from abuse by the majority.[150] Although this history is often used to argue against the modern doctrine of regulatory takings,[151] this Part applies it to the question of discharging claims for just compensation after a taking (regardless of what kind of taking occurred and whether recognizing such a taking is consistent with history). After first providing an overview of the original understanding of the two-tier Takings Clause, this Part argues that making takings claims dischargeable follows from this understanding.

A. History of the Two-Tier Takings Clause

The Takings Clause, as a compromise between competing ideologies, was designed to have a two-tier structure—it would activate and provide strong protections of property rights in areas involving a special risk of process failure, but would otherwise be

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149 *See infra* Part III.A.

150 *See infra* Part III.B.

151 *See, e.g.*, Treanor, *supra* note 36, at 804–05.

merely an instructional tool.[152] Professor William Treanor has described how the original understanding of the Takings Clause reflected a compromise between two ideologies at the time of the Framing: (1) "Lockean liberalism, which treats the right to property as prepolitical," and (2) "republicanism, which values the right to property but subjects it to majoritarian delineation."[153] While generally the Takings Clause would merely serve a "hortatory function" and be a rhetorical tool for criticizing the government's treatment of property rights, it created a bar on the government directly possessing property without compensation out of a "concern that the political process would not fairly consider certain possessory interests."[154] Specifically, those who ratified the Takings Clause were likely most immediately concerned by the possibility of military impressment of personal property.[155] Whereas normally the structure of the national government could be trusted to adequately protect property rights through extensive deliberation and vetogates, military action during war would lack these procedural safeguards and thus require a bright-line rule protecting property rights against abuse.[156]

This understanding of the two-tier Takings Clause has broader roots in the postrevolutionary U.S. experience.[157] Debates about the taking of property initially were dominated by a republican perspective: although there was a general presumption in favor of compensating owners for taken property, the main focus was on ensuring that a "republican decisionmaking body, normally a jury or the legislature," was positioned to weigh the facts and decide whether "compensation was consistent with the public good."[158] The introduction of categorical just compensation requirements—first in state constitutions and then in the Takings

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152 Treanor, *supra* note 36, at 837; *see also* John F. Hart, *Colonial Land Use Law and Its Significance for Modern Takings Doctrine*, 109 HARV. L. REV. 1252, 1287–99 (1996); John F. Hart, *Land Use Law in the Early Republic and the Original Meaning of the Takings Clause*, 94 NW. U. L. REV. 1099, 1131–47 (2000) (offering a historical analysis that complements Treanor's and offers supporting historical evidence); *cf.* John E. Fee, *The Takings Clause as a Comparative Right*, 76 S. CAL. L. REV. 1003, 1007 (2003) (offering an analysis of the Takings Clause in antidiscrimination terms as being about protecting individuals "where the government legitimately targets merely one or few owners").

153 Treanor, *supra* note 36, at 818.

154 *Id.* at 819.

155 *Id.* at 835–36.

156 *Id.*

157 *See id.* at 834.

158 Treanor, *supra* note 36, at 825.

Clause of the Fifth Amendment—represented a limited break with this republican tradition.[159] Such requirements bolstered liberal property rights that could trump majoritarian decision-making in narrow areas "in which the political process was unlikely to consider property claims fairly."[160] For instance, the Vermont Constitution of 1777 created a just compensation requirement for the taking of real property out of a concern that rural populations living far away from the state's political elite would be treated unfairly (which was an especially salient threat given Vermont's experience as part of New York).[161] Similarly, the Massachusetts Constitution of 1780 created a just compensation requirement out of a concern that the military would seize property and thus was focused on process failures arising during wartime.[162]

This historical background informed the drafting and ratification of the Takings Clause. The two-tier Takings Clause would protect property against the government when there was a high likelihood of process failure but otherwise would merely be a tool for debate in the broader range of cases where democratic majorities could be trusted to make decisions.[163] Although there were different understandings of what counted as the relevant process failures—from Vermont's and Massachusetts's specific fears about abuse from concentrated political centers and soldiers to Madison's more general (and condemnable) fears "about majoritarian confiscation of land and slaves"—the underlying thought was the same: the Takings Clause would be at its strongest in areas where the normal procedural and political safeguards against governmental abuse could not be trusted for some particular reason.[164] Otherwise, majoritarian institutions would get significant leeway.[165] This two-tier understanding similarly informed the drafters of the Fourteenth Amendment, which incorporated the Takings Clause against the states. They were similarly concerned with "protecting the property interests of a

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159 *Id.* at 825–27.

160 *Id.* at 854.

161 *Id.* at 827–30.

162 *Id.* at 830–32.

163 Treanor, *supra* note 36, at 855; *see also* William Baude, *Rethinking the Federal Eminent Domain Power*, 122 YALE L.J. 1738, 1793–96 (2013) (discussing the original purpose of the Takings Clause along similar lines).

164 Treanor, *supra* note 36, at 855.

165 *Id.*

group that was isolated from the normal give and take of the political process," and otherwise envisioned that the Takings Clause would take a backseat.[166]

Insofar as the Takings Clause's underlying history and purpose ought to guide novel legal questions about the Takings Clause—like that of the dischargeability of takings claims—they suggest the following basic test: there should be a general presumption in favor of letting majoritarian institutions act based on their own understanding of how to balance property rights with the public good, but individual rights need stronger protection against majoritarian institutions when there is a particularly high threat of process failure. The key to knowing how the Takings Clause applies thus requires knowing whether there is some special risk of process failure.

B. Applying the Two-Tier Takings Clause

This historical account of the two-tier Takings Clause can be used to answer whether the right to just compensation after a taking should be dischargeable in bankruptcy. Of course, given that the first municipal bankruptcy statutes were not passed until the 1930s,[167] it is unlikely that anyone from the Founding or Reconstruction Eras would have well-developed thoughts about how the interest in just compensation from the Takings Clause should interact with municipal bankruptcy. Nevertheless, the historical understanding of the two-tier Takings Clause can be applied to this context by asking whether the discharge of takings claims in municipal bankruptcy involves a high risk of process failure.[168] If it does, then the Takings Clause's protections should be at their peak; otherwise, its protections should be much weaker. Thus, our key question is whether takings creditors can rely on the normal mechanics of government, through procedure and politics, to guard against being abused by a discharge or instead are like civilians in wartime or rural farmers in Vermont who need an added safeguard against abuse.

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[166] *Id.* at 862. *But see* Michael B. Rappaport, *Originalism and Regulatory Takings: Why the Fifth Amendment May Not Protect Against Regulatory Takings, but the Fourteenth Amendment May*, 45 SAN DIEGO L. REV. 729, 756 (2008) (giving reasons to be alert to potential differences in the understanding of the Takings Clause as drafted and as understood during incorporation).

[167] Michael W. McConnell & Randal C. Picker, *When Cities Go Broke: A Conceptual Introduction to Municipal Bankruptcy*, 60 U. CHI. L. REV. 425, 450 (1993).

[168] *See supra* Part III.A.

In the context of discharging takings claims, there seems to be one obvious source of process failure. Insofar as takings creditors already suffered from some kind of process failure that prevented them from protecting their property from being taken through ordinary politics, the same process failures will be at play when the government tries to discharge the takings claim. For example, consider the takings creditors in Detroit who owned property near the airport.[169] One might plausibly fear that the same process failures that prevented them from adequately protecting their property from the City—namely, the fact that they were a relatively small and unorganized group—would prevent them from adequately protecting their takings claims in bankruptcy. But the risks of process failure against takings creditors in municipal bankruptcy are significantly dampened by its host of safeguards, which guard against the possibility that takings creditors are singled out and abused in bankruptcy.

The first safeguard comes from the requirements for a municipality to file for bankruptcy in the first place. To be eligible for municipal bankruptcy, a municipality must be specifically authorized under state law.[170] This requirement puts the state government in a position to serve as an extra safeguard against abuse by the municipality. Additionally, municipalities can file for municipal bankruptcy only when insolvent,[171] and courts have understood this requirement to be quite restrictive.[172] Courts heavily police municipalities from using bankruptcy proactively and require municipalities to wait until their "coffers are near empty," to the point that they cannot service short-term debt.[173] Such restrictions greatly (arguably to the point of excessive caution) limit the circumstances in which a municipality can use bankruptcy opportunistically to abuse politically weak takings creditors and instead restrict bankruptcy to situations where the municipality has a legitimate need for it.

Then, within bankruptcy proceedings themselves, there are many procedural safeguards to protect takings creditors. To give

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169 *See supra* text accompanying notes 13–14.

170 *In re City of Detroit*, 524 B.R. at 160; *see also* 11 U.S.C. § 109(c)(2).

171 11 U.S.C. § 109(c)(3).

172 Vincent S.J. Buccola, *The Logic and Limits of Municipal Bankruptcy Law*, 86 U. CHI. L. REV. 817, 823–25 (2019).

173 *Id.* at 825.

a few examples, there are extensive notice requirements,[174] creditors can present objections to the confirmation of the plan,[175] and the bankruptcy court has broad equitable powers to dismiss a petition[176] or deny confirmation of the plan[177] if the municipality is acting in bad faith. Moreover, a presumption in favor of treating similar (from the perspective of nonbankruptcy law) creditors equally helps guard against specific abuses against takings creditors.[178] It is thus no accident that the takings creditors within the three relevant cases in Detroit, Stockton, and Puerto Rico were treated as general unsecured creditors and did not receive any specific targeting as takings creditors.[179] Because takings creditors will generally be lumped into a broad coalition of unsecured creditors, they will have significantly more power to use ordinary politics—through coalitions with the many other unsecured creditors—to guard against abuse from the political process.

All this is to say, the multitude of formal and informal safeguards within municipal bankruptcy will make it highly likely (though not guaranteed) that the interests of takings creditors are accounted for and protected from the worst kinds of abuse. Indeed, there is reason to think that municipal bankruptcy's discharge of takings claims is just part of an overall scheme to make the best out of a bad situation for the community, generally leaving takings creditors no worse off than they would be without municipal bankruptcy.[180] At the very least, municipal bankruptcy falls outside the narrow set of cases where process failure is likely and the force of the Takings Clause should be at its peak. Thus, provided the safeguards within municipal bankruptcy remain robust, the original two-tier understanding of the Takings Clause lines up well with making takings claims dischargeable.

IV. NORMATIVE CONSIDERATIONS

Besides formalism and history, the most compelling reasons to permit the discharge of takings claims are normative. This Part

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[174] *See* 6 COLLIER ON BANKRUPTCY ¶ 923.01 (Alan N. Resnick & Henry J. Sommer eds., 16th ed. 2017).

[175] *See id.* ¶ 943.01.

[176] *See id.* ¶ 930.01.

[177] *See id.* ¶ 943.03.

[178] *See* Richard M. Hynes & Steven D. Walt, *Inequality and Equity in Bankruptcy Reorganization*, 66 U. KAN. L. REV. 875, 875–76 (2018).

[179] *See supra* notes 15, 59, 89, and accompanying text.

[180] *See infra* Part IV.B.

begins by taking a bird's-eye view that asks which legal treatment of takings claims would have the best societal consequences. But one still may have serious normative concerns about whether making takings claims dischargeable unduly harms takings creditors. In trying to determine whether takings creditors are harmed, this Part will proceed from the starting point that the normatively relevant counterfactual comparison is a world without municipal bankruptcy. Using this world without bankruptcy as the baseline, this Part shows that takings creditors are very unlikely to be harmed—and, if anything, are often helped by municipal bankruptcy, discharge and all. This gives further reason to think discharge is constitutionally permissible in the first place given the lack of substantial harm.[181]

A. Societal Consequences

Based on the societal consequences—where we table for now any harm to takings creditors—making takings claims dischargeable is normatively attractive. On one hand, the major argument against making takings claims dischargeable is that doing so allows municipal bankruptcy to become an end run around the Takings Clause and threatens to place costs that the public should bear on specific property owners.[182] But the countless safeguards in municipal bankruptcy, discussed in Part III.B, guard considerably against the risk of abuse in municipal bankruptcy.[183] On the other hand, the most obvious consideration against immunizing takings claims from discharge is that doing so can often

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[181] *Cf.* Faitoute Iron & Steel Co. v. City of Asbury Park, 316 U.S. 502, 503–07, 512–16 (1942) (*superseded by statute*, 60 Stat. 415, *as recognized by* Puerto Rico v. Franklin Cal. Tax-Free Trust, 579 U.S. 115 (2016)) (putting substance over form in a Contracts Clause challenge to a state bankruptcy statute). In *Faitoute Iron*, Justice Felix Frankfurter, writing for the Court, rejected a Contracts Clause challenge to a state bankruptcy statute discharging a municipality's obligations to pay an unsecured bondholder. *Id.* at 512–13. Justice Frankfurter emphasized that given the precarious character of the bonds before the discharge, interpreting the Constitution as protecting the paper value of the bonds "is . . . mak[ing] the Constitution a code of lifeless forms instead of an enduring framework of government for a dynamic society." *Id.* at 516. He insisted that "[t]he Constitution is 'intended to preserve practical and substantial rights.'" *Id.* at 514 (quoting Davis v. Mills, 194 U.S. 451, 457 (1904)). Analogously, the fact that takings creditors are not substantially harmed by municipal bankruptcy (discharge and all) suggests constitutional protections are not implicated.

[182] *See* Brief in Opposition to a Petition for a Writ of Certiorari Filed by Suiza Dairy, Corp. at 4, Fin. Oversight & Mgmt. Bd. for Puerto Rico v. Coop. de Ahorro y Credito Abraham Rosa, 143 S. Ct. 774 (2023) (No. 22-367).

[183] *See supra* text accompanying notes 170–79.

threaten the very viability of municipal bankruptcy and the prospect of financial recovery because of the need to pay takings claims in full.[184]

Still, there are more subtle considerations that cement the bottom-line conclusion that society at large would benefit from making takings claims dischargeable. In a legal regime where takings claims get special treatment, claimants will be incentivized to characterize their claims as takings claims "as far as normative argument and innovative lawyering allows."[185] This has already happened in Puerto Rico since *In re Financial Oversight & Management Board*. For example, credit unions argued that a claim against Puerto Rico inducing them to invest in worthless government-issued bonds, which more naturally would be classified as an ordinary tort claim, qualified as a protected takings claim.[186] Such litigation threatens to spiral as the Supreme Court adds uncertainty about what counts as taking.[187] Relatedly, introducing an asymmetry in how tort liability and takings liability are discharged creates perverse incentives for the government to try acquiring property through torts rather than through formal condemnation processes.[188]

Additionally, when takings claims are immunized from discharge and contractual obligations are not, courts will face a new problem about how to treat settlement agreements concerning takings disputes. Courts can follow the First Circuit and find that such settlement agreements do not receive protection against discharge.[189] Doing so, however, threatens to chill claimants from

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184 *See* Petition for Writ of Certiorari, *supra* note 30, at 23.

185 *See* Mark Lammey, Note, *Finding a Port in the Storm: Constitutional Claims Find Protection Under the Fifth Amendment in Municipal Bankruptcy in* In re Financial Oversight & Management Board, 68 VILL. L. REV. 291, 329 (2023).

186 *In re* Fin. Oversight & Mgmt. Bd. for Puerto Rico, 54 F.4th 42, 59–60 (1st Cir. 2022).

187 *See supra* note 34 and accompanying text. While making takings claims dischargeable might increase litigation about whether takings claims are secured, these controversies can be resolved through fairly mundane state property law, which almost certainly will be clearer than the Supreme Court's opaque takings doctrine.

188 *See* Petition for Writ of Certiorari, *supra* note 30, at 21; Arpan A. Sura, Note, *End-Run Around the Takings Clause—The Law and Economics of* Bivens *Actions for Property Rights Violations,* 50 WM. & MARY L. REV. 1739, 1782 (2009) (describing how the government can be incentivized to rely on torts, including extended schemes of harassment and trespass, to induce owners to transfer property to get around the Takings Clause).

189 *See In re* Fin. Oversight & Mgmt. Bd. for Puerto Rico, 79 F.4th 95, 105–07 (1st Cir. 2023).

making settlement agreements over takings disputes when municipalities risk financial insolvency. When a municipality is insolvent and about to enter bankruptcy, why settle a takings claim and lose valuable protections against discharge? This chilling threat will be particularly substantial because private parties will struggle to assign a price to the protection against discharge and will worry about negotiating when the municipality has significantly more information about the likelihood it will enter bankruptcy. Alternatively, discharging settlement agreements over takings claims risks complicated litigation about how to classify settlement agreements—which often will turn on complicated factual questions about the nature of the underlying disputes. This option also risks chilling municipalities from making settlement agreements over anything that could plausibly be classified as a takings claim, given that those settlements could be fully immunized from discharge. That is, once takings claims receive special protections against discharge, there is no good way to treat settlements over takings claims.

In addition to avoiding these thorny legal problems, takings claims ought to be dischargeable in order to make it easier for municipalities to use municipal bankruptcy. While municipal bankruptcy suffers from a host of problems, it still has the potential to be a powerful tool for financial recovery.[190] If anything, our municipal bankruptcy regime suffers from being too inaccessible—which, as a consequence, means communities cannot access municipal bankruptcy until it is too late to avoid irreparable economic and societal harms from high debt burdens.[191] When the next housing crisis or pandemic happens and our communities take on large amounts of debt,[192] municipal bankruptcy will hopefully be there to help our communities recover. A questionable interpretation of the Takings Clause should not stand in the way.

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[190] *See* Buccola, *supra* note 172, at 821 (describing how municipal bankruptcy can help municipalities recover from financial distress and more broadly contribute to economic efficiency by removing the distortive effects of debt).

[191] *Id.* at 863–66.

[192] *See, e.g.*, Aurelia Chaudhury, Adam J. Levitin & David Schleicher, *Junk Cities: Resolving Insolvency Crises in Overlapping Municipalities*, 107 CALIF. L. REV. 459, 470 (2019) (describing how "[e]ven in metropolitan areas with relatively stable economies, a combination of political and legal forces—in particular the decline of local political parties and weakening legal restrictions on local budgeting—has shaped overlapping governments in ways that increase the likelihood of fiscal crises"); DAVID SCHLEICHER, IN A BAD STATE: RESPONDING TO STATE AND LOCAL BUDGET CRISES 77–118 (2023) (describing municipal fiscal crises from the Great Recession in 2008 through the COVID-19 pandemic).

B. Harm to the Takings Creditors

Relative to a counterfactual where takings creditors get all the benefits of municipal bankruptcy while also being protected from discharge, takings creditors are clearly harmed if their claims become dischargeable. But this harm has minimal moral significance. Takings creditors—like all of us—have no right to receive optimal treatment from a bankruptcy regime where they get all of the benefits and none of the costs. As a more plausible baseline, this Section will assume that takings creditors merely have a moral right not to be harmed by municipal bankruptcy.[193] If municipal bankruptcy as a whole leaves takings creditors no worse off, then takings creditors have little moral standing to complain about their claims being discharged. Discharge would simply be the tax that takings creditors pay into the bankruptcy system, which would at the very least be matched by the correlative benefits they received from bankruptcy. Thus, this Section will use a counterfactual without municipal bankruptcy as a baseline to determine whether takings creditors are harmed in a morally problematic way by getting their claims discharged. Working with this baseline, this Section shows that municipal bankruptcy—even with discharge—leaves takings creditors generally no worse off for two main reasons. In the best-case scenario, municipal bankruptcy can actively generate value for the takings creditor by helping the municipality access crucial investments that will increase the pot of resources available to creditors. But even in the worst-case scenario where municipal bankruptcy cannot fix a municipality's economic problems, it still leaves a takings creditor no worse off than the perilous place they would be in without bankruptcy—and in fact bankruptcy likely provides an efficient way to make the most out of a bad situation. The upshot of this analysis is that takings creditors have no moral standing to object to discharge because the bitter of bankruptcy is more than offset by the sweet.

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[193] This assumption is likely too simple to be true, strictly speaking. Even if takings creditors are made no worse off by the municipal bankruptcy regime, they still may cite concerns about fairness—if, for example, the net benefits from the bankruptcy regime are not being shared equally. Nevertheless, especially given that municipal bankruptcy has the procedural safeguards described in Part III.B to guard against abuses, there are reasons to think municipal bankruptcy will be roughly fair in its distributional effects.

Consider a takings creditor trying to recover their claim from a financially insolvent municipality in a world without bankruptcy.[194] One useful way to understand the creditor's options is to examine the existing legal landscape in 1933, before the first federal and state municipal bankruptcy statutes were enacted.[195] Professors Michael McConnell and Randal Picker outlined the legal remedies that were then available to a takings creditor seeking to recover a takings judgment from an insolvent municipality. As a matter of state statute and common law, these remedies were the following: (1) seizure of city property; (2) judicial oversight of city financial affairs, including limitations on expenditures that would divert funds away from debt service; (3) seizure of private property within the city; (4) state assumption of municipal indebtedness; (5) acquisition of a lien on future tax revenues; and (6) imposition of new taxes earmarked for debt service.[196]

Despite this range of theoretical possibilities, "only the last avenue was usually available in actual practice," with the other options being either "legally unavailable," "limited to special circumstances, requir[ing] special authorization, or [ ] of little practical use."[197] The remaining sixth option involved a creditor asking a court to issue "a writ of mandamus requiring imposition of new taxes" that the municipality would be required to use to pay their debt.[198] Nevertheless, this remedy would often be available only for contractual debts.[199] Even if a creditor were to obtain a judgment against the municipality through mandamus, "a city could indefinitely postpone payment of noncontractual obligations by the simple stratagem of appropriating all revenues to other public purposes."[200] This scarcity of legal remedies, other than perhaps the use of mandamus, remains the case today.[201]

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194 Specifically, the focus of this Comment is on a takings creditor with an unsecured takings claim. *See supra* Part I.A (explaining this qualification).

195 *See* McConnell & Picker, *supra* note 167, at 427.

196 *Id.* at 429.

197 *Id.* at 429, 445.

198 *Id.* at 445.

199 *Id.* at 448.

200 McConnell & Picker, *supra* note 167, at 448. To some extent, this kind of indefinite delay is still possible. *Id.* at 448 n.99; *see* Evans v. City of Chicago, 873 F.2d 1007, 1010–11 (7th Cir. 1989) (describing Chicago's permissible practice of paying tort judgments with only specially earmarked taxes, resulting in payments of some judgments delayed "as long as nine years").

201 *See* Omer Kimhi, *Reviving Cities: Legal Remedies to Municipal Financial Crises*, 88 B.U. L. REV. 633, 647–50 (2008) (describing how "[i]n the municipal context, . . . even if

Even in contexts where creditors *could* use mandamus, there would be "serious practical drawbacks" to using it during "times of general financial distress" because of collective action problems.[202] If a single creditor files a suit, it can "trigger an avalanche of suits by [other creditors] who do not wish to be last in line."[203] Trying to recover through the mandamus thus can trigger a vicious cycle. Higher taxes lead to more delinquency and encourage the tax base to leave the jurisdiction, requiring even higher taxes that exacerbate these problems and end up "effectively destroy[ing] the fiscal base of the city."[204] At the end of this vicious cycle, the creditor is left with no ability to effectively recover their claim as they try to force the municipality to squeeze water from a stone. While in principle creditors could try to negotiate some optimal level of recovery through mandamus that would avoid triggering these vicious cycles, holdout problems generally prevent such agreements.[205] Moreover, even today, a court using mandamus generally "may not force a locality to increase its taxes above any limits prescribed in the state's statutes, and the creditors can use only the surplus of the revenues the municipality receives above the amount it needs for the local operating expenses."[206] For these reasons, Justice Felix Frankfurter observed that "the right to enforce claims against the city through mandamus is the empty right to litigate."[207]

All this is to say that when a municipality is suffering from financial distress, the takings creditor is left with an extremely limited ability to recover anything close to their full claim in a world without municipal bankruptcy. This limitation is only exacerbated by considerations from public choice theory. Takings creditors will often be small and relatively unorganized political groups, who will struggle to effectively lobby for their rights compared to much larger and more organized groups of creditors like pensioners or public employees.[208]

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the creditors receive a favorable judgment against a locality, their ability to enforce the judgment is very limited").

202 *See* McConnell & Picker, *supra* note 167, at 448.

203 *See id.*

204 *See id.*

205 *Id.* at 449.

206 Kimhi, *supra* note 201, at 649.

207 *Faitoute Iron*, 316 U.S. at 510.

208 *See, e.g.*, Saul Levmore, *Just Compensation and Just Politics*, 22 CONN. L. REV. 285, 311 (1990) (arguing that the government will not harm large interest groups without offering something in return).

On the other side of the ledger, there are reasons to think that municipal bankruptcy can actively help takings creditors relative to the counterfactual without bankruptcy. Professor Vincent Buccola has developed a model in which the core economic function of municipal bankruptcy is preserving certain spatial economies—"the properties of a physical location that make people and firms want to locate there"—which are threatened by excessive public debt.[209] While in a "Coasean nirvana" investors could bargain around a municipality's debt to preserve the spatial economies generated by a municipality's infrastructure, in our world with transaction costs, excessive "debt can lead to underinvestment, both public and private, in infrastructure within a municipality's territorial limits."[210] Municipal bankruptcy can lower a municipality's debt level, allowing it to preserve valuable spatial economies through, for example, repairing roads and having well-funded schools.[211] In doing so, municipal bankruptcy avoids the deadweight losses that occur from failures to invest in a community.[212] These gains in efficiency then can translate into the municipality having more money to pay creditors back.

The beneficial effects of municipal bankruptcy for the constitutional creditor will be strongest when the municipality merely suffers from "financial distress"—i.e., when, if not for high debt leading to underinvestment, it would have an economically viable package of services and revenue.[213] During financial distress, municipal bankruptcy can increase the pot of resources available to pay creditors by allowing the municipality to effectively access the investment needed for its viable economic model.[214] While all the creditors are harmed on paper by having their claims discharged, this is offset by the fact that removing the crippling effects of high debt puts the municipality in a better position to pay back the creditors than it otherwise would have been in. Bankruptcy thus can increase the size of the pie by enabling the municipality to make valuable investments. In doing so, municipal bankruptcy ultimately helps get more money to put into the hands of creditors. Takings creditors, who often own nontaken land within the

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209 Buccola, *supra* note 172, at 820–21.

210 *Id.* at 832–33.

211 *See id.* at 820.

212 *See id.*

213 *See id.* at 839–40.

214 *See* Buccola, *supra* note 172, at 844.

municipality, will receive further residual benefits from bankruptcy through the increase in land value from the preservation of spatial economies.[215]

On the other hand, when a municipality faces "economic distress"—i.e., when it would have no economically viable package of services and revenue even absent high debt—it is less clear that municipal bankruptcy will affirmatively benefit the takings creditor.[216] During economic distress, high levels of debt are not the cause of a municipality's problems but are a symptom of a broader economic problem.[217] Here, there is no reason to think that reducing a municipality's debt burden will put it in a position to have more resources to pay creditors back. Nevertheless, it is still unlikely that a constitutional creditor would be harmed by municipal bankruptcy in this context given that a municipality in economic distress with unsustainable debt can quickly "find[ ] itself unable to raise revenues sufficient to cover basic services such as police, fire, and sanitation" and likely will prioritize funding such services or paying back more politically powerful creditors as opposed to paying takings creditors.[218] Takings creditors here face the prospect of recovering very little in a world without bankruptcy, so it is unclear that a world where their claims are discharged is any worse.

In summary, takings creditors are rarely harmed by municipal bankruptcy relative to a counterfactual without bankruptcy. While discharge harms their claims on paper, such creditors would generally be able to recover far less than this paper value in a world without bankruptcy given their limited legal and political abilities. In the best-case scenario, municipal bankruptcy can actively help such creditors by enabling the municipality to expand the pot of resources it has to pay creditors back through enabling key investments. But even when a municipality faces more

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[215] *See id*. at 820.

[216] *Id.* at 839. Given the restrictive filing requirements, municipalities generally will not be able to file for municipal bankruptcy when they merely face financial distress; instead, they will have to wait until financial distress metastasizes into economic distress and causes irreparable harm. *Id.* at 854–55. This is one crucial reason why the legal regime should make municipal bankruptcy, on the margin, easier for municipalities to enter—which, as this Comment has argued, can and should include making takings claims eligible for discharge.

[217] *Id.* at 833. For example, technological changes might cause a massive production shock by making a community's predominant industry no longer viable. *See* Buccola, *supra* note 172, at 842.

[218] *Id.* at 843.

intractable economic problems, municipal bankruptcy is still likely better than the alternative, where constitutional creditors would be wasting legal fees as they compete with much more powerful groups to recover what they can from the sinking ship.

At the very least, whether takings creditors are harmed by municipal bankruptcy as a whole is considerably complex, and any overall harm is likely marginal. Of course, one might think that takings creditors should have more legal recourse in a world without bankruptcy. But the upshot of that point is that nonbankruptcy law has flaws and should be changed to give takings creditors more legal rights. Unless or until takings creditors get more rights outside of bankruptcy, municipal bankruptcy—and its discharge of takings claims—is not the source of the harm.[219] It is thus a mistake to think of discharge as some unfair harm to takings creditors. Instead, discharge is an essential part of a broader scheme where municipal bankruptcy tries to make the best out of a bad situation.

Most importantly, it should be clear that the relatively small risk of harm to takings creditors is significantly outweighed by the positive consequences of letting takings claims be discharged. Making takings claims dischargeable, with an (at worst) small harm to takings creditors, avoids erecting a barrier that would make it considerably harder (if not impossible) for our communities to use a powerful tool for financial recovery. Making takings claims dischargeable is thus not only legally correct—it is the right thing to do.

CONCLUSION

The major contribution of this Comment has been to develop an argument from first principles—that fills in the major hole of the Ninth Circuit's analysis—about why takings claims can constitutionally be discharged in municipal bankruptcy. The argument has proceeded in three parts. First, this Comment undermined the formalist case for immunizing takings claims from discharge by revealing that it rests on questionable assumptions about the nature of the right to just compensation. Second, this Comment demonstrated that the Takings Clause was originally understood as operating with a two-tier model where individual

[219] Of course, one still might criticize municipal bankruptcy for not solving (or counteracting) problems in nonbankruptcy law. But using bankruptcy to solve nonbankruptcy problems likely will run into problems in the way two wrongs often fail to make a right.

property rights are protected in areas that risked process failure, but otherwise majorities would get deference. Because the procedural and political safeguards attending municipal bankruptcy guard against abuse, the Takings Clause should be at its nadir, permitting takings claims to get discharged. Finally, this Comment showed that normative considerations favor making takings claims dischargeable: doing so benefits society writ large and does not cause any objectionable harm to those whose claims would get discharged.

As communities across the country inevitably struggle with fiscal crises, a categorial ban on discharging takings claims threatens to weaken an already significantly restricted tool for recovery. The damage from immunizing takings claims could in fact decimate municipal bankruptcy as the Roberts Court expands what counts as a taking. Fortunately, immunizing takings claims from discharge is not mandatory. Nothing in the Takings Clause—either as a formal matter or from its history—requires giving takings claims special protection from the normal goings-on of municipal bankruptcy. It is up to us, not the Takings Clause, whether we keep the door to financial recovery open.