3-1-1983

The Impairment of Secured Creditors’ Rights in Reorganization: A Study of the Relationship Between the Fifth Amendment and the Bankruptcy Clause

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Some commentators and courts have argued that the takings clause of the fifth amendment limits congressional power to interfere with property rights in bankruptcy proceedings. In this Article, Professor Rogers argues to the contrary that, at least with respect to prospective bankruptcy legislation, the bankruptcy clause itself and not the fifth amendment limits congressional bankruptcy power. His view derives from nineteenth and twentieth century case law, particularly cases assessing the validity of restraints on secured creditors' foreclosure rights, and from the theoretical difficulty of distinguishing between supposedly protected property rights and supposedly unprotected contract interests. Professor Rogers also sharply criticizes the Supreme Court's analysis in the recently decided Security Industrial Bank case, which concerned the extent to which fifth amendment principles limit retroactive application of bankruptcy legislation.

ARTICLE I, section 8 of the Constitution provides that "[t]he Congress shall have Power . . . [t]o establish . . . uniform Laws on the subject of Bankruptcies throughout the United States."¹ As the concept of bankruptcy is now understood and implemented,² this clause confers authority on the federal government to adopt far-reaching measures to deal with the problems of insolvent or otherwise financially troubled individuals and enterprises. Through the exercise of this

¹ U.S. Const. art. I, § 8.
² The currently effective federal bankruptcy law is the Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549 (codified at 11 U.S.C., in scattered sections of 28 U.S.C., and in scattered sections of other titles (Supp. V 1981)), which became generally effective on October 1, 1979, for bankruptcy cases commenced on or after that date, id. §§ 401-403, 92 Stat. at 2682-83. The Bankruptcy Reform Act of 1978 is hereinafter referred to as the "Bankruptcy Code." The prior federal bankruptcy law, that is, those provisions repealed by id. § 401, 92 Stat. at 2682, is referred to as the "Bankruptcy Act."
power, the federal government may assume control over the assets and affairs of a debtor, disregarding all manner of contractual and property rights of creditors and other investors, and encourage or force the parties interested in the debtor's affairs to accept in satisfaction of their claims an entirely different package of rights than that for which they had originally bargained. Other provisions of the Constitution, however, appear to limit the power of government to disrupt private economic rights: "No State shall . . . pass any . . . Law impairing the Obligation of Contracts";3 "No person shall . . . be deprived of . . . property, without due process of law";4 "nor shall private property be taken for public use, without just compensation."5

Because exercise of the bankruptcy power substantially impairs private property and contract rights, some accommodation must be reached between the affirmative grant of power in the bankruptcy clause and the limitations found in the fifth amendment and related provisions. It is the purpose of this Article to consider how these constitutional provisions can be reconciled. Although the subject is, at the most general level, the relationship between the bankruptcy clause and the fifth amendment, much of the discussion centers on a narrower issue — the source and nature of constitutional limits on impairment of secured creditors' rights during the pendency of reorganization proceedings.6 The reason for this focus is that the problem of interim restraint of secured creditors' rights is perhaps the only issue concerning the constitutional limits of the bankruptcy power that has received much attention in recent times.7 Part I of this Article presents and criticizes the

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3 U.S. CONST. art. I, § 10. For a discussion of the application of contracts clause principles to federal legislation, see infra pp. 989–91.

4 U.S. CONST. amend. V.

5 Id.

6 Problems concerning secured creditors' rights to reclaim collateral from debtors involved in bankruptcy proceedings are most acute in reorganization proceedings rather than in liquidation or "straight" bankruptcy proceedings. Accordingly, the discussion in this Article focuses on reorganization proceedings, although the conclusions reached concerning the extent to which the Constitution restricts Congress' ability to impair secured creditors' rights apply equally to straight bankruptcy cases in which secured creditors' foreclosure rights might be restrained.


7 The literature on the treatment of secured creditors' rights in reorganization is extensive. For case citations, see 2 COLLIER ON BANKRUPTCY ¶ 362.01 (L. King 15th ed. 1982) [hereinafter cited as COLLIER]; 6 COLLIER ON BANKRUPTCY ¶ 3.32 (J.
currently dominant model of constitutional constraints on bankruptcy legislation, a model under which fifth amendment principles limit the substantive scope of the bankruptcy power. Part II develops a different and more satisfactory model under which the sole source of substantive limits on the bankruptcy power is the bankruptcy clause itself. Part III considers whether special constitutional problems are presented by retroactive bankruptcy legislation.

Before beginning the analysis, a basic understanding of reorganization is required. The central assumption of the reorganization provisions of federal bankruptcy law is that the value of an enterprise as a going concern will often exceed the liquidation value of the enterprise's assets. Reorganization proceedings are designed to preserve this going concern surplus for the benefit of the enterprise's creditors and investors by providing a breathing spell during which the enterprise may assess its affairs, effect economies in its operations, and attempt to reorder its financial structure free from the necessity of dealing with the immediate demands of its creditors.

In nearly all cases, the debtor's business operations must be continued for the reorganization effort to succeed, and continued operations may require that the debtor be permitted


9 For convenience, this Article refers to the entity operating the business during reorganization as "the debtor" rather than a more precise but cumbersome phrase such as "debtor in possession or trustee."
to use property in which creditors hold security interests. The secured creditors, however, will undoubtedly have the right by virtue of their agreements with the debtor and the relevant state law to seize the collateral securing their claims and sell it off to satisfy the debts secured. In cases in which accommodation between the debtor and the secured creditors cannot be reached by negotiation, the reorganization court will need to decide whether to restrain the secured creditor from exercising his rights against the collateral during the pendency of the proceedings.\footnote{Similar issues are presented when the debtor seeks a turnover order requiring a secured creditor to turn over collateral in the creditor's possession for use in the operations of the debtor during reorganization, see Bankruptcy Code §§ 362, 542, 11 U.S.C. §§ 362, 542 (Supp. V 1981), or when the debtor seeks authority to issue certificates of indebtedness secured by liens with priority over existing security interests, see id. § 364, 11 U.S.C. § 364. For discussion of such issues in the context of turnover orders, see In re Third Ave. Transit Corp., 198 F.2d 703 (2d Cir. 1952); Coogan, Broude & Glatt, supra note 7, at 1169–78; Countryman I, supra note 7, at 316–20; Countryman II, supra note 7, at 351–54; for a discussion of the issues in the context of certificates of indebtedness, see Baker, Certificates of Indebtedness in Reorganization Proceedings: Analysis and Legislative Proposals, 50 AM. BANKR. L.J. 1 (1976).}

A restraint, of course, will subject the secured creditor to the risk that, if the reorganization effort fails and if the value of the collateral has declined during the pendency of the proceedings, he may find himself in a worse position than he would have occupied had he been allowed to exercise his rights at the outset.\footnote{A reorganization court would, however, authorize such an impairment of secured creditors' rights only if persuaded that a successful reorganization were likely. In the event of a successful reorganization, the secured creditor can be given a package of cash and securities equal in value to the amount of its secured claim at the inception of the proceedings, see In re Yale Express Sys., 384 F.2d 990, 992 (2d Cir. 1967), in which event the secured creditor would not have been harmed by the order in question. Even if the effort to reorganize fails, the secured creditor can be granted some measure of protection by giving him a priority claim for the amount of any reduction in the value of the collateral. See id. By successful reorganization, I mean simply the consummation of a plan of reorganization providing at least for the payment of the claims of secured creditors in accordance with the applicable requirements of federal bankruptcy law. In general, a plan may be approved, at least over the objections of creditors, only if it complies with the "absolute priority rule." Very roughly, the absolute priority rule requires that, before any distribution to junior claimants is permissible, a plan of reorganization must give secured creditors a package of cash and securities of the reorganized company having a value equal to the value of the secured creditors' claims against the property of the debtor. See Consolidated Rock Prods. Co. v. Du Bois, 312 U.S. 510, 520–21 (1941); Case v. Los Angeles Lumber Prods. Co., 308 U.S. 106, 116 (1939); Northern Pac. Ry. v. Boyd, 228 U.S. 482, 504–05 (1913). For discussion of the extent to which the Bankruptcy Code has incorporated the requirements of the absolute priority rule, see Klee, All You Ever Wanted To Know About Cram Down Under the New Bankruptcy Code, 53 AM. BANKR. L.J. 133 (1979).}
I. THE UNCONSTITUTIONAL IMPAIRMENT THESIS

Perhaps more by dint of repetition than by analysis, it seems to have become an accepted proposition of reorganization law that the fifth amendment limits the extent to which secured creditors may be subjected to the risk of loss due to restraint of their foreclosure rights. Virtually every discussion of the problem includes a reference to Justice Brandeis' statement in *Louisville Joint Stock Land Bank v. Radford* that "[t]he bankruptcy power, like the other great substantive powers of Congress, is subject to the Fifth Amendment."¹³ The theory that the fifth amendment places substantive limits on the ability of the government to restrain secured creditors' rights in reorganization has crystallized into the following proposition: any impairment of the liquidation value of a secured creditor's collateral attributable to the exercise of powers conferred on the reorganization court by bankruptcy legislation is, in the absence of just compensation, a violation of the takings clause of the fifth amendment.¹⁴ For convenience, this proposition is referred to in this Article as the Unconstitutional Impairment Thesis.

Although the Unconstitutional Impairment Thesis evolved at a time when the text of the bankruptcy statutes provided very little guidance on the permissibility of restraining secured

¹⁴ Judge Cyr's comments in *In re American Kitchen Foods*, 2 BANKR. CT. DEC. (CRR) 715 (Bankr. D. Me. June 8, 1976), are typical:

The fifth amendment to the United States Constitution guarantees protection against any taking of private property even for a wholly public use without just compensation. *Louisville Joint Stock Land Bank v. Radford*, 295 U.S. 555, 602 (1935). The peripheral scope of the just compensation clause encompasses collateral impairments resulting from government restraints upon the exercise of contract rights acquired by a secured creditor in specific property of its debtor. *Id.* No material impairment of collateral is constitutionally permissible, either within or without bankruptcy proceedings, in the absence of just compensation.

No unconstitutional impairment is occasioned where the value recoverable from the collateral remains sufficient to satisfy the indebtedness secured. *Wright v. Union Central Insurance Co.*, 311 U.S. 273, 278 (1940). Similarly, where the stay complained of has resulted in no diminution, no collateral impairment can have occurred and no constitutional issue is posed.

*Id.* at 719 (citations and footnote omitted).

For convenience, I refer to the Unconstitutional Impairment Thesis as a requirement that the value of the collateral be preserved, though to be more precise, one should speak of a requirement of preserving the value of the secured party's interest in the collateral. Thus, even under the Unconstitutional Impairment Thesis, no constitutional issue would be presented by diminution in the value of collateral held by an oversecured creditor as long as the value of the collateral remained in excess of the amount of the debt. See 2 COLLIERT, *supra* note 7, ¶ 362.01, at 362-15.
creditors' rights, the widespread acceptance of the Thesis seems to have had a substantial impact on the evolution of the present statutory law of reorganization. The new Bankruptcy Code contains detailed provisions specifying the extent to which impairment of secured creditors' rights is permissible during the pendency of bankruptcy proceedings, the key being the concept of adequate protection. Although the term "adequate protection" is not defined, section 361 of the Bankruptcy Code contains a nonexclusive list of possible techniques for providing adequate protection. For example, as compensation for any depreciation in the value of collateral that may result from a given order, a secured creditor can be granted either a substitute lien on other property of the debtor or periodic cash payments. Section 361(3), however, explicitly states that it is not sufficient simply to give secured creditors an unsecured claim having priority as an expense of administration as compensation for the amount of any loss in the value of their collateral. Thus, under the adequate protection provisions of the Bankruptcy Code, a secured creditor cannot be forced to rely solely on the court's assessment that the debtor's earning power will be adequate to ensure repayment of the debt even if the collateral depreciates or is dissipated. Rather, any risk of loss occasioned by diminution of the value of the collateral during the pendency of the proceedings must be eliminated by giving the secured creditor substitute collateral or its equivalent in cash. The adequate protection model, therefore, precisely mirrors the supposed constitutional requirements of the Unconstitutional Impairment Thesis.

If, as this Article argues, the Unconditional Impairment Thesis is entirely unsound, a major aspect of the new Bankruptcy Code's treatment of reorganization problems may be based, to some extent, on a foundation of sand. Given that the present statutory law of reorganization has largely incorporated the supposed requirements of the Unconstitutional Impairment Thesis, rejection of the Thesis may not have major

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15 For discussion of the relevant problems of statutory interpretation under the old Bankruptcy Act, see Countryman I, supra note 7; Murphy I, supra note 7, at 27-45; Webster, supra note 7.
17 Id. § 361, 11 U.S.C. § 361.
18 Id. § 361(3), 11 U.S.C. § 361(3).
19 Indeed, the legislative history makes it quite clear that the adequate-protection model is derived, at least in part, from what Congress assumed to be a constitutional requirement concerning the protection of secured creditors' property interests. See S. REP. No. 989, 95th Cong., 2d Sess. 49, reprinted in 1978 U.S. CODE CONG. & AD. NEWS 5787, 5835; H.R. REP. No. 595, supra note 8, at 339, reprinted in 1978 U.S. CODE CONG. & AD. NEWS at 6295.
immediate impact. Yet unless the flaws of the Thesis are exposed, many possible proposals for amending the present reorganization provisions will be doomed from the outset by the assumption that the proper treatment of secured creditors' rights in reorganization is dictated by constitutional requirements rather than by policy considerations that are within the discretion of Congress.

A. Precedent for the Unconstitutional Impairment Thesis

1. The Frazier-Lemke Act Cases. — The principal source of authority for the Unconstitutional Impairment Thesis is a series of Supreme Court decisions involving amendments to the Bankruptcy Act that were enacted by the Frazier-Lemke Act of 1934.20 The Frazier-Lemke Act, which applied only to debts existing at the time of its enactment,21 was designed to assist farmers who faced the prospect of losing their farms through mortgage foreclosure. The Act affected mortgagees in two major respects. First, it enabled the debtor to obtain a stay of foreclosure proceedings for a period of five years, during which time the debtor was to remain in possession, paying rent in an amount fixed by the court for distribution among the secured and unsecured creditors as their interests appeared.22 Second, at any time during the five-year period, the debtor could acquire full title to the mortgaged real estate by paying the mortgagee the appraised value of the real estate.23 The practical effect of the latter provision was that the mortgagee might be deprived of the right to conduct a foreclosure sale at which he could bid in the amount of his debt and thereby obtain full title to the property in the hope that future increases in its value might enable him more fully to obtain repayment of his claim.

In Louisville Joint Stock Land Bank v. Radford,24 the Supreme Court, in a unanimous opinion authored by Justice Brandeis, held the Frazier-Lemke Act unconstitutional. Although the precise basis of the ruling is not entirely clear, the case has been widely interpreted to hold that the Frazier-Lemke Act violated the takings clause of the fifth amendment by taking from a mortgagee without compensation rights that

22 Id.
23 Id.
he otherwise would have had to the mortgaged premises. In response to the *Radford* decision, Congress amended the Frazier-Lemke Act. Two years after *Radford*, the Supreme Court upheld the revised Act in *Wright v. Vinton Branch of the Mountain Trust Bank*, another unanimous opinion by Justice Brandeis.

It is by no means easy to discern the principle that enabled Justice Brandeis to conclude that the changes made by Congress in response to *Radford* sufficed to overcome the constitutional objections found fatal in that case. Congress' changes in the two key provisions of the Act were, in fact, rather insubstantial. First, with respect to the stay imposed by the original Act, the revised Act simply shortened the period of the stay from five to three years. It is true that in *Vinton Branch* Justice Brandeis read the revised Act to provide that the stay could be terminated if it appeared that the debtor would be unable to rehabilitate himself within the three-year period, but on this point *Vinton Branch* was expressly repudiated by the Court two years later in *John Hancock Mutual Life Insurance Co. v. Bartels*.

Second, as it was ultimately interpreted, the revised Act did not change significantly the provision denying the mortgagee the right to acquire the property through a judicial sale. Although in *Vinton Branch* Justice Brandeis interpreted the revised Act to direct that a judicial sale be held if the debtor failed to pay rent or comply

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The concluding language of Justice Brandeis' opinion offers some support for this reading:

The province of the Court is limited to deciding whether the Frazier-Lemke Act as applied has taken from the Bank without compensation, and given to Radford, rights in specific property which are of substantial value. As we conclude that the Act as applied has done so, we must hold it void. For the Fifth Amendment commands that, however great the Nation's need, private property shall not be thus taken even for a wholly public use without just compensation. If the public interest requires, and permits, the taking of property of individual mortgagees in order to relieve the necessities of individual mortgagors, resort must be had to proceedings by eminent domain; so that, through taxation, the burden of the relief afforded in the public interest may be borne by the public.

295 U.S. at 601–02 (citations omitted).


27 300 U.S. 440 (1937).


29 300 U.S. at 462.

30 308 U.S. 180, 184 & n.3 (1939).
with other court orders,31 three years later, in *Wright v. Union Central Insurance Co.*, the Court ruled that even in such circumstances the statute gave the debtor the opportunity to redeem the property for its appraised value before a judicial sale could be conducted.32

2. Relevance of the Frazier-Lemke Act Cases to the Unconstitutional Impairment Thesis. — The most plausible explanation of the irreconcilability of *Radford* and the subsequent Frazier-Lemke Act cases is that the later cases overrule or substantially undercut the vitality of *Radford*.33 Courts and commentators, however, have often stated that the subsequent Frazier-Lemke Act cases only refined the principles developed in *Radford*34 and that certain dicta in *Union Central* express the determinative principle — that the mortgagee is constitutionally entitled to have the value of the property preserved and devoted to the payment of his debt. On this view, the reason that the revised Act was upheld is that it preserved to the mortgagee this constitutional minimum. Thus, Patrick Murphy, an authority on reorganization law, reads *Union Central* to have established that “the secured creditor has a distinct property interest which is entitled to constitutional protection throughout the proceeding” and that the core of this protected property interest is the right to have the value of the collateral preserved.35 Similarly, the most recent edition of the Collier treatise reviews the Frazier-Lemke Act cases and concludes that *Union Central* contains “the clearest statement of a right of a secured creditor, namely, to have the value of its secured position maintained throughout the proceedings.”36 The Frazier-Lemke Act cases, that is, are taken to establish the validity of the Unconstitutional Impairment Thesis.

Even if *Radford* survives the subsequent Frazier-Lemke Act cases, it is difficult to see how the Frazier-Lemke Act cases support the position of the Unconstitutional Impairment Thesis.

31 *Vinton Branch*, 300 U.S. at 461–62.
33 Indeed, the Supreme Court itself once admitted that it may have fallen into error in *Radford* and corrected itself in *Vinton Branch*. See *Helvering v. Griffiths*, 318 U.S. 371, 400–01 & n.52 (1943).
that preservation of the value of collateral is the key constitutional right of the secured creditor. The literature contains several suggestions of the ways in which the original Frazier-Lemke Act may have failed to provide protection against possible depreciation in the value of the mortgagee's interest in the property; none of these possibilities, however, appears to have played any significant role in the Frazier-Lemke Act cases. Some interpreters of Radford have suggested, for example, that the basis of the ruling was that the mortgagee was not protected against erosion of his position due to the possible accumulation of tax liens having priority over the mortgage.\(^{37}\) Yet in Radford the parties stipulated that the annual charges for taxes and insurance were $105, and the rental fixed by the court was $325 during the first year.\(^{38}\) Although the original Act did not explicitly provide that taxes were to be paid from the rentals, the court of appeals assumed that such payment was contemplated,\(^{39}\) and nothing in Justice Brandeis' opinion suggests the contrary. Even if there were serious dispute on this question, or even if the rental had been fixed at a level inadequate to pay taxes or other prior charges as they accrued, it strains credulity to suppose that Justice Brandeis would have held an act of Congress unconstitutional on such grounds in the face of the obvious alternative of interpreting the statute to require that rentals be fixed at a level adequate to pay taxes and be so applied. After all, it was Justice Brandeis who, less than a year after the Radford decision, delivered the well-known dissertation on the virtues of avoiding unnecessary constitutional decisions in his Ashwander concurrence.\(^{40}\)

Others who read Radford to have established the Unconstitutional Impairment Thesis suggest that the constitutional vice of the Frazier-Lemke Act was the possibility that the collateral might decline in value during the period of the stay.\(^{41}\) Yet there was essentially no discussion of this point in Radford, and there appears to have been no evidence before the Supreme Court in Radford suggesting that any depreciation in the value of the collateral was likely. Furthermore, with respect to the possibility of decline in the value of the collateral, the Frazier-Lemke Act was indistinguishable from the Min-


\(^{38}\) Radford, 295 U.S. at 577-78.


\(^{41}\) See, e.g., Chicago Comment, supra note 7, at 517.
nesota Mortgage Moratorium Act, which had been upheld by the Court only a year before in *Home Building & Loan Association v. Blaisdell.* One would hardly expect that Congress' explicitly granted power to deal with problems of financially troubled debtors is restricted by fifth amendment principles in a more rigorous fashion than the general police powers of the states to deal with similar matters are restricted by fourteenth amendment or contracts clause principles.

Commentators who read the Frazier-Lemke Act cases to have established the Unconstitutional Impairment Thesis seem to rely primarily on the *Union Central* opinion, in which Justice Douglas, in the course of describing the revised Act, stated that “[s]afeguards were provided to protect the rights of secured creditors, throughout the proceedings, to the extent of the value of the property” and that “[t]here is no constitutional claim of the creditor to more than that.” Although Justice Douglas' comments are consistent with the proposition that a secured creditor is constitutionally entitled to have the liquidation value of the collateral preserved, there is little reason to suppose that Justice Douglas had such a proposition in mind. His comments concerning the safeguards provided to protect the mortgage were made in the course of ruling, as a matter of statutory interpretation, that even a debtor who failed to pay rent required by order of the court was entitled to the opportunity to buy the property at its appraised value. Thus, the most plausible interpretation of his comments in *Union Central* is that Justice Douglas was not addressing the notion that preservation of the value of collateral is a constitutional requirement, but instead was rejecting the suggestion

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44 It is true that the revised Act upheld in *Vinton Branch* and *Union Central* contained a provision, not included in the original Act, authorizing courts to require mortgagors to make payments of principal in addition to rent if such payments were necessary to preserve security. Pub. L. No. 74-384, § 75(b)(3), 49 Stat. 942, 944. An adherent of the Unconstitutional Impairment Thesis might argue that this provision was the change that saved the revised Act, for by requiring payments of principal, a court might protect a secured creditor from loss caused by diminution in the value of the collateral. Yet given the absence of any suggestion in *Radford* that the possibility of depreciation was the significant constitutional flaw in the original Act, there is little reason to suppose that this amendment was the saving grace in the revised Act.
45 See, e.g., 2 COLLIER, supra note 7, ¶ 362.01, at 362-15; Murphy II, supra note 7, at 1491.
46 Id.
in Radford and Vinton Branch that the mortgagee is constitutionally entitled to the opportunity of obtaining title to the property itself by bidding in the amount of his debt at a foreclosure sale.

The most fundamental flaw in the suggestion that Radford supports the Unconstitutional Impairment Thesis is the irrelevancy of that case to the central assertion of the Thesis, that the fifth amendment imposes definite constitutional limitations on the substance of bankruptcy legislation. It seems to be thought that fifth amendment principles derived from Radford impose generally applicable limits on the substantive scope of bankruptcy power of a sort that would apply even to purely prospective bankruptcy legislation. For example, during the lengthy legislative process that culminated in the enactment of the new Bankruptcy Code, numerous commentators seriously considered whether the proposed bills' treatment of secured claims comported with the requirements of the fifth amendment, yet nothing in this literature suggests that these commentators saw the problem as one limited to security interests in existence at the time the proposed legislation was to be enacted. Congress appears to have shared this conception. The House and Senate reports on the adequate protection provisions of the bills, citing Radford and Union Central, state that the concept of adequate protection is derived from the requirements of the fifth amendment. The reports lack any indication that the constitutional issue was seen to be limited to problems of retroactivity. Similarly, in cases decided before the enactment of the new Bankruptcy Code that discuss the Unconstitutional Impairment Thesis, the theory must have been that the vague language of the old Bankruptcy Act could not be interpreted to confer power to impair secured creditors' rights in a fashion inconsistent with the Unconstitutional Impairment Thesis, because Congress would have lacked power to adopt such a statute explicitly.

Radford and its progeny, however, provide no support at all for the assertion of such a broad substantive limit on the powers of Congress under the bankruptcy clause. If we are to make any sense out of Radford, we need to note the precise point in the opinion at which Justice Brandeis made the famous statement that the bankruptcy power is subject to the

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48 See supra note 19.
fifth amendment.\textsuperscript{49} Immediately before this statement, Justice Brandeis was discussing the mortgagee's contention that Congress lacks power to “attempt, by a bankruptcy act, to abridge, solely in the interest of the mortgagor, a substantive right of the mortgagee in specific property held as security.”\textsuperscript{50} Justice Brandeis stated, however, that “we have no occasion to decide [that issue] in this case.”\textsuperscript{51} He then noted that the Frazier-Lemke Act applied only to preexisting mortgages, and stated that, “[b]ecause the Act is retroactive in terms and as here applied purports to take away rights of the mortgagee in specific property, another provision of the Constitution is controlling.”\textsuperscript{52} Then comes the statement that the bankruptcy power is subject to the fifth amendment.\textsuperscript{53}

In context, Justice Brandeis' comments suggest that the holding of the case is only that the modification of secured creditors' rights effected by the Frazier-Lemke Act was too substantial to permit the Act to be applied retroactively.\textsuperscript{54} Thus, the famous statement that the bankruptcy power is subject to the fifth amendment must be taken to mean nothing more than that the fifth amendment, through either the due process or the takings clause, is the constitutional foundation for the proposition that statutes that retroactively disrupt settled expectations may be subject to particularly attentive judicial scrutiny.\textsuperscript{55} Hence, even if \textit{Radford}'s specific application of retroactivity concepts survived the subsequent Frazier-Lemke Act cases, and even if those cases could be read to support the notion that preservation of the value of a secured creditor's collateral is a matter of constitutional significance in the context of retroactive application of statutes, none of the Frazier-Lemke Act cases provides any support whatsoever for the proposition that fifth amendment property-protection concepts limit the substantive scope of the bankruptcy power.

\textsuperscript{49} 295 U.S. at 589.
\textsuperscript{50} Id.
\textsuperscript{51} Id.
\textsuperscript{52} Id.
\textsuperscript{53} Id.
\textsuperscript{54} The decisions upholding the revised Frazier-Lemke Act, \textit{Vinton Branch} and \textit{Union Central}, might then be explained on the ground that, even though both cases involved retroactive application of the Act to preexisting mortgages, see \textit{Union Central}, 311 U.S. at 275 (referring to earlier decision in Wright v. Union Cent. Life Ins. Co., 304 U.S. 502, 504-05 (1938), for statement of facts); \textit{Vinton Branch}, 300 U.S. at 454, the revised Act effected a less extensive modification of the mortgagees' rights than did the original Act. Given the relatively minor nature of the changes made by the revised Act, however, it is probably more realistic to view the revised Act cases to have essentially overruled \textit{Radford}'s particular application of fifth amendment retroactivity principles.
\textsuperscript{55} See infra Part III.
B. Theoretical Flaws in the Unconstitutional Impairment Thesis

Lack of support for the Unconstitutional Impairment Thesis in the Frazier-Lemke Act cases does not, in itself, demonstrate that the Thesis is invalid. It is necessary, therefore, to consider whether there is any independent theoretical support for the Thesis. There are two constitutional provisions that appear to be plausible candidates as textual support for the notion that the bankruptcy power is limited by the requirement of nonimpairment of secured creditors’ property rights: the due process clause and the takings clause. The due process clause is, today, hardly an appealing candidate. The contention that the due process clause is the source of the Unconstitutional Impairment Thesis reduces to the claim that rather freewheeling Lochner-style economic substantive due process should be revived. In light of the glee with which the Supreme Court seizes every available opportunity to repudiate Lochner yet again, few are likely to pursue that route. Accordingly, adherents of the Unconstitutional Impairment Thesis seem to rely on the takings clause. That avenue, however, proves on careful examination to be no less troublesome.

1. Retroactivity, Prospectivity, and the Takings Clause. — Much of the intuitive appeal of the Unconstitutional Impairment Thesis probably is traceable to the assumption that the decision made by a reorganization court during bankruptcy proceedings is the “taking” of which the secured creditor complains. Before initiation of reorganization proceedings, the secured creditor had the right to seize the collateral upon the debtor’s default. Once the debtor has entered reorganization proceedings, however, the court may refuse to permit the creditor to exercise his foreclosure right, and may instead allow the debtor to use the property during the course of the reorganization. Thus, it seems only natural to describe what has happened as a taking by the government (in the person of the bankruptcy court) of the secured creditor’s property (the collateral) for public use (pursuit of the public policy of promoting reorganization) without any compensation for possible losses.

The appeal of this view is entirely illusory. Except in situations in which an amendment to bankruptcy law is applied retroactively — that is, to a secured financing arrange-

ment entered into before adoption of the amendment — all that happens when a reorganization court stays a secured creditor from foreclosing on his collateral is that the court applies a preexisting rule of law to a specific case. What, one may ask, has been “taken” from the secured creditor? At the time he entered into the security arrangement, he knew or should have known that his rights were circumscribed by the federal legislation. If his property rights are defined by reference to existing law, obviously no taking has occurred. Thus, the proposition that the fifth amendment imposes limitations on even purely prospective restrictions of the rights of secured creditors seems to assume that the property rights held by secured creditors are in some sense anterior to positive law. The implications of that concept are staggering. Obviously the numerous provisions of state and federal law that restrict a creditor’s ability to obtain an enforceable security interest cannot all be unconstitutional as takings of private property without just compensation. Yet the effort to determine which rights are the natural entitlement of secured creditors is a task that strikes the modern legal mind as futile if not simply incomprehensible.

58 The matter of constitutional limits on retroactive application of newly enacted bankruptcy legislation is discussed in infra Part III.

59 In the context of unsecured creditors’ rights, the notion that the contracts clause might restrict prospective legislation was rejected long ago. In 1819, the Supreme Court held in Sturges v. Crowninshield, 17 U.S. (4 Wheat.) 122 (1819), that a state insolvency law that provided for the discharge of debts incurred prior to the enactment of the statute violated the contracts clause. Eight years later, however, in Ogden v. Saunders, 25 U.S. (12 Wheat.) 213 (1827), the Court ruled that, because the obligations of contracts are defined and limited by positive state law, no constitutional problem is presented by prospective insolvency acts. To be sure, Sturges and Ogden involved the rights of unsecured creditors. As is discussed below, however, see infra pp. 988–95, there is little reason to believe that the constitutional rights of secured creditors in bankruptcy are substantially different from those of unsecured creditors. In any event, the logical problems presented by the suggestion that purely prospective legislation may violate the takings clause are exactly the same as those involved in the contracts clause setting in Ogden.

I am inclined to suggest that no takings clause issue can ever be presented by a truly prospective statute. One might object that such a thesis would mean that the government could entirely avoid the just compensation requirement by simply announcing in advance, for example, that all interests in real property were thereafter held subject to the government’s right to take land without compensation for schools, roads, fire stations, and the like. On the other hand, most takings clause cases involve real estate, and given the old saw of real estate brokers that “they’re not making it anymore,” it is hard to imagine how legislation restricting the use of land could ever be truly prospective. As soon as the government announced that a certain use of land would henceforth be prohibited or that certain land might be taken without compensation at some time in the future, the value of the affected land would be diminished, to the detriment of its current owner. There can be no new land; there can, however, be new security arrangements.
Alternatively, an adherent of the Unconstitutional Impairment Thesis might resort to notions of federalism to explain the way in which a prospective federal statute can amount to a taking. The argument would be that, although prospective state legislation raises no takings problems, prospective federal legislation may not impair state-created property rights absent just compensation. This theory, however, is wholly unsatisfactory, for it assumes that the takings clause restricts federal legislation more severely than it does state legislation. Nothing in the case law or commentary on the takings clause supports such a view. The takings clause does far more than restrict federal legislation impairing property rights defined by state law. At least since the 1896 case of *Chicago, Burlington & Quincy Railroad v. Chicago*, it has been clear that the takings clause requirements are applicable to the states through the fourteenth amendment. Thus, the just compensation requirement embodies a limitation on the power of government generally and not a limitation on the powers of the federal government with respect to state-created property rights.

Although the rather thorny problems posed by the notion that fifth amendment principles limit even prospective bankruptcy legislation probably suffice to dispose of the Unconstitutional Impairment Thesis, it may be appropriate to consider other theoretical flaws in the Thesis. 61

2. The Distinction Between Secured and Unsecured Creditors. — The Unconstitutional Impairment Thesis cannot be maintained without drawing a sharp distinction between the

60 166 U.S. 226 (1896).
61 There may be reason to feel slightly reluctant about using the implausibility of the notion of a prospective taking as the sole basis for rejecting suggestions that fifth amendment concepts limit the substantive scope of governmental powers. First, the distinction between retroactive and prospective legislation is not entirely clear-cut. Legislation prohibiting child labor, for example, is prospective in the sense that it regulates employment relationships only from the date of its enactment, but is retroactive to the extent that it may invalidate prior employment contracts or, more broadly, to the extent that it may reduce the value of business enterprises that had been established on the assumption that child labor would be permitted. Thus, whether a legislative measure is taken to effect a retroactive impairment of settled expectations depends on the breadth of one's conception of the relevant expectations. Second, one must be a bit careful with the notion that constitutional problems concerning the disruption of property or contract rights can be avoided by defining the rights solely by reference to existing positive law; pushed to the extreme, such a theory would enable government to announce, as a postulate of the positive law, that all rules are subject to change, and would thereby render nugatory any constitutional provision protecting expectations of property or contract rights. See L. Tribe, *American Constitutional Law* § 9-6, at 468–69 (1978). The limited concept of the prospective-retroactive distinction needed to refute the Unconstitutional Impairment Thesis does not, however, seem to come even close to presenting such problems.
constitutional rights of secured creditors and those of unsecured creditors. Exercise of the bankruptcy power clearly entails substantial impairments of the rights of unsecured creditors, the clearest instance being the grant of a discharge to the debtor. The constitutionality of such impairments of unsecured creditors' rights, however, has long been settled. Thus, unless some substantial basis exists for distinguishing the constitutional rights of secured creditors from those of unsecured creditors, the ready acceptance of impairments of unsecured creditors' rights in bankruptcy must cast grave doubt on the validity of the Unconstitutional Impairment Thesis.

Although unsecured creditors' rights against the debtor are generally described as contractual rights, this characterization alone cannot explain why impairment of unsecured creditors' rights in bankruptcy has not been viewed to pose substantial constitutional problems. First, the Supreme Court on a number of occasions has explicitly stated that contractual rights are a species of property protected by the due process and takings clauses. Second, modern developments in the area of procedural due process protections of entitlements to government benefits and employment are hardly consistent with

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62 Moreover, the Thesis is not even consistent in its solicitude for the rights of creditors holding liens against property of the debtor. As Professor Countryman has noted, see Countryman I, supra note 7, at 335, the proposition that secured creditors are constitutionally entitled to receive the full value of their collateral is hard to square with the numerous provisions of bankruptcy law that declare various sorts of liens unenforceable. Enforceable state-created property rights of creditors in specific property of the debtor are routinely "taken" by the operation of provisions of the bankruptcy law dealing with preferential transfers, fraudulent conveyances, judicial liens, tax liens, landlord liens, and the like. See Bankruptcy Code §§ 545, 547-548, 724, 11 U.S.C. §§ 545, 547-548, 724 (Supp. V 1981). Courts have routinely rejected the suggestion that such impairments of otherwise valid liens are unconstitutional. See, e.g., In re Jay & Dee Store Co., 37 F. Supp. 989, 991 (E.D. Pa. 1941) (landlord's lien); In re Glover Casket Co., 1 F. Supp. 743 (N.D. Ga. 1932) (tax lien); In re Rhoads, 98 F. 399, 402 (W.D. Pa. 1899) (judicial liens); cf. First Nat'l Bank v. Staake, 202 U.S. 141, 148 (1906) (whether state-created judicial liens should be enforced in bankruptcy is a matter committed to Congress' discretion); Egyptian Supply Co. v. Boyd, 117 F.2d 608, 611 (6th Cir. 1941) (same).

63 E.g., Hanover Nat'l Bank v. Moyses, 186 U.S. 181, 188 (1902); In re Klein, 14 F. Cas. 716 (C.C.D. Mo. 1843) (No. 7865).

64 E.g., United States Trust Co. v. New Jersey, 431 U.S. 1, 19 n.16 (1977) (takings clause); Lynch v. United States, 292 U.S. 571, 579 (1934) ("The Fifth Amendment commands that property not be taken without making just compensation. Valid contracts are property . . . . [T]he due process clause prevents the United States from annulling them . . . . "); Sinking Fund Cases, 99 U.S. 700, 718-19 (1879) (due process clause).

65 E.g., Bishop v. Wood, 426 U.S. 341, 344 (1976) ("A property interest in employment can, of course, be created by ordinance or an implied contract."); Perry
a narrow interpretation of the fifth amendment that would exclude contractual rights from the scope of the term "property." Moreover, although the contracts clause is by its terms applicable only to the states, commentators have often noted that the due process clause of the fifth amendment has essentially the same effect in the context of federal legislation. In any event, the Court has never suggested that, merely because the fifth amendment refers to "property" and the contracts clause by its terms applies only to the states, there is no basis for constitutional challenges to federal legislation impairing contractual rights. Quite the contrary, such landmark cases


68 There are, to be sure, statements in some bankruptcy cases to the effect that federal bankruptcy legislation impairing unsecured creditors' rights is constitutionally unproblematic simply because the contracts clause applies only to the states. E.g., Kuehner v. Irving Trust Co., 299 U.S. 445, 451-52 (1937); Louisville Joint Stock Land Bank v. Radford, 295 U.S. 555, 589 (1935); In re American Kitchen Foods, Inc., 2 BANKR. CT. DEC. (CRR) 715, 719 (Bankr. N.D. Me. June 8, 1976). For the reasons explained in the text, however, such statements are quite misleading. The Supreme Court has at times spoken more accurately about the applicability of contracts clause principles to the federal government. See Continental Ill. Nat'l Bank & Trust Co. v. Chicago, R.I. & Pac. Ry. (Rock Island), 294 U.S. 648, 680-81 (1935), quoted at infra pp. 1006-07.

The true meaning of the thought inaptly captured by the statements to the effect that the contracts clause is not applicable to the federal government may be simply that the bankruptcy clause represents a transfer from the states to the federal government of the authority to exercise the historic power of sovereign states to alter or abrogate, for legitimate reasons of public policy, the rights of creditors against their debtors. As has been related many times, the contracts clause was adopted against a background of extensive colonial and state legislation for the relief of debtors. The theory of the contracts clause may be that the exercise of such power by the individual states endangered the union and the maintenance of a sound system of credit and commerce. The remedy adopted by the Constitution, however, was not to remove from all government the power to alleviate the situation of debtors by impairing the obligation of contracts, but rather to transfer that authority to the federal government with the requirement that it be exercised uniformly: "The Congress shall have Power . . . [t]o establish . . . uniform Laws on the subject of Bankruptcies throughout the United States . . . ." U.S. CONST. art. I, § 8. This theory was suggested by Justice Catron, sitting on circuit, in the leading case of In re Klein, 14 F. Cas. 716, 718 (C.C.D. Mo. 1843) (No. 7865). The argument might well lead one to the conclusion, however, that the states are barred altogether from enacting insolvency or bankruptcy acts, whether retroactive or prospective. Indeed, a variant of this argument was used by Chief Justice Marshall in his dissenting opinion in Ogden v. Saunders, 25 U.S. (12 Wheat.) 213 (1827), in support of his conclusion, contrary to that of the majority, that the contracts clause prohibits the states from enacting even prospective insolvency acts. See id. at 354 (Marshall, C.J., dissenting).
of constitutional law as the *Legal Tender Cases*\(^6^9\) and the *Gold Clause Cases*\(^7^0\) involved the constitutional problems posed by federal legislation impairing contractual rights.\(^7^1\)

Even if constitutional protection were limited to "property" rights, it is by no means clear that unsecured creditors' rights against a debtor's estate would fail to qualify as such to the same extent as secured creditors' liens. It is true that, unlike secured creditors, unsecured creditors have no specific interest in any particular portion of the debtor's assets. Unsecured creditors do, however, have legally recognized interests in the debtor's assets as a whole. Through various forms of process specified by state debtor-creditor law, virtually all of a debtor's assets may be reached to satisfy the demands of his creditors. Furthermore, state debtor-creditor law is replete with provisions designed to protect unsecured creditors' rights in the debtor's assets. Fraudulent conveyance law is, of course, the prime example, though analogous concepts can be found in related bodies of law such as bulk sales laws, restrictions on dividend payments by corporations, and the like.\(^7^2\) In a loose sense, therefore, the debtor's property is "a trust fund charged primarily with the payment of [the debtor's] liabilities."\(^7^3\)

Reliance on the labels "property" and "contract," therefore, hardly suffices to explain the supposed distinction between the constitutional rights of secured and unsecured creditors. The task thus is to identify more precisely the differences between secured and unsecured creditors' rights and to consider whether these differences warrant the conclusion that different constitutional principles apply in the two fields.

An unsecured creditor's legal right against the debtor can be divided into two components: obligation and remedy. The obligation is the debtor's personal liability to repay the debt. It is an obligation that the legal system generally stands ready to enforce, except to the extent that the bankruptcy system permits the debtor to obtain a discharge. The remedy is execution or similar process specified by state law, pursuant to which the unsecured creditor can cause property of the debtor to be seized and sold in order to satisfy the claim. The secured creditor's legal right against the debtor can be divided into the same two components. There is no difference


\(^7^1\) See Norman, 294 U.S. at 304-05, 307-08; Knox, 79 U.S. (12 Wall.) at 475.


\(^7^3\) Northern Pac. Ry. v. Boyd, 228 U.S. 482, 504 (1913).
between the rights of secured and unsecured creditors with respect to the obligation. As in the case of unsecured creditors' rights, the legal system's readiness to enforce the debtor's personal liability to the secured creditor is qualified by the discharge provisions of bankruptcy law. The difference between secured creditors' rights and unsecured creditors' rights lies in the remedy: the secured creditor has identified in advance of default the property to be seized and sold in satisfaction of his claim.\(^{74}\) The law stands ready to enforce the secured creditor's right to have this property seized and sold, and if the secured creditor has taken the necessary perfecting steps,\(^{75}\) the legal system will recognize his claim to this property to have priority over most other interests in the property.\(^{76}\)

That the secured creditor has preselected the particular property to be devoted to the satisfaction of his claim seems to play a strong role in the contention that secured creditors' "property" rights are a matter of special constitutional significance.\(^{77}\) Curiously, however, the identity of the specific property involved is perhaps the matter of least importance to the secured creditor. The secured creditor has no concern about the collateral per se. Rather, the secured creditor's concerns are only that the collateral have and retain sufficient value to satisfy his claim and that it be readily salable — the same concerns that unsecured creditors have about the debtor's property in general.Indeed, the preselection of the property to be devoted to repayment of his claim is one aspect of the secured creditor's remedial rights that even adherents of the Unconstitutional Impairment Thesis seem to concede may be impaired in bankruptcy. Under sections 361–364 of the Bank-

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\(^{74}\) The notion that the secured creditor's remedial right is a "property" right may derive much of its intuitive force from the perception of the mortgage on Blackacre as the paradigm of secured financing. Secured financing law, however, has become far more complex. One of the most significant forms of modern secured financing — and the form that often presents the most difficult problems in reorganization — is financing on the security of the inventory or accounts receivable of an enterprise. The collateral in such arrangements is more of an accounting concept than a specific piece of property. Once we move from a mortgage on Blackacre to a floating lien, see U.C.C. §§ 9-204 to -205 (1977), on accounts, the "property rights" perspective becomes blurred. The remedial right of the secured creditor in an accounts receivable financing arrangement is the right, upon the debtor's default, to have the debtor's contractual claims against others paid to the creditor rather than to the debtor or other creditors of the debtor. Id. § 9-502. The arbitrariness of classifying such a sophisticated bundle of rights as either "property" or "contract" belies the suggestion that decisions of constitutional significance should be based on the classification.

\(^{75}\) E.g., id. §§ 9-302 to -306.

\(^{76}\) E.g., id. §§ 9-201, -301, -312.

\(^{77}\) See, e.g., Murphy I, supra note 7, at 23.
bankruptcy Code, which appear to have been drafted to comply with the supposed requirements of the Unconstitutional Impairment Thesis, a bankruptcy court may freely take away a secured creditor's rights against his specific collateral and substitute a lien on other property of the debtor having equal value. An argument for the Unconstitutional Impairment Thesis that is premised on the fact that the secured creditor has preselected the property to be devoted to his claim is therefore curious indeed. Notwithstanding the premise that preselection of specific assets is constitutionally significant, the argument admits that the claim to specific assets can freely be disregarded, and shifts without explanation to the supposed conclusion that only the value of that property must be preserved.

The specificity of the secured creditor's claim against the debtor's property is therefore a matter of neither practical nor constitutional significance. Rather, the factor that distinguishes secured creditors' rights from those of unsecured creditors is that, as a matter of state law, the secured creditor's claim ranks above those of the unsecured creditors. It is difficult, however, to see why the particular position of the secured creditor in the ranking of claims against the debtor's property is entitled to constitutional protection not enjoyed by claimants occupying different ranks. To be sure, as a matter of state law concerning creditors' rights, secured creditors rank above unsecured creditors, and unsecured creditors rank above ownership interests. Yet if the essence of the secured creditor's right is simply his priority ranking, why should it be thought, as the Unconstitutional Impairment Thesis contends, that any significant disruption of ranking that affects secured creditors is a matter of major constitutional significance while a disruption of priority ranking that affects other claimants — for example, that effected by granting a discharge — is entirely unproblematic?

I am inclined to suspect that the notion that secured creditors are entitled to far greater constitutional protection than are unsecured creditors rests on nothing more than a confusion.

78 See supra p. 978.
79 See Coogan, The New Bankruptcy Code: The Death of Security Interest?, 14 GA. L. REV. 153, 162-66 (1980); cf. Consolidated Rock Prods. Co. v. Du Bois, 312 U.S. 510, 530 (1941) ("If the creditors are adequately compensated for the loss of their prior claims, it is not material [for the purposes of the absolute priority rule] out of what assets they are paid.").
80 Both the discharge and the exemption provisions enable individual debtors, whose claims to their assets are analogous to those of the shareholders of a corporation, to retain assets despite creditors' prior claims to the property.
between the nature of secured creditors' claims and the particular form that our legal system has evolved for the implementation of those claims. Perhaps solely as a matter of historical accident, the system of risk allocation embodied in secured financing arrangements has been implemented through the mechanism of granting to the creditor a property interest in certain assets of the debtor. There is, however, no logical necessity about this choice of mechanism. One can imagine a system of "secured" financing that would be functionally identical to the current system but that would rest simply on a scheme of contractual priorities. Contractual agreements might provide that some percentage of the debtor's assets be devoted exclusively to the claims of a particular "secured" creditor, so that the secured creditor would have to share with the general creditors only the balance of the estate. To protect this contractual allocation of risk from disruption by a decrease in the value of the debtor's entire estate, the contracts might provide that the "secured" creditor could immediately begin collection proceedings if the value of the debtor's assets dropped below some specified value. Had such a system evolved, I doubt that anyone would be inclined to regard the fifth amendment to have particularly greater relevance to the question whether this system of contractual priorities could be modified in reorganization proceedings than to the question whether other contractual rights may be impaired in reorganization.

If all that distinguishes the secured from the unsecured creditor is that the secured creditor has sought to protect himself from risks of nonpayment through contractual arrangements concerning the debtor's property, Chief Justice Hughes' comment in the *Gold Clause Cases* provides a complete answer to the secured creditor's contention that his "property" rights entitle him to special constitutional protection: "Contracts may create rights of property, but when contracts deal with a subject matter which lies within the control of the Congress, they have a congenital infirmity. Parties cannot remove their transactions from the reach of dominant constitutional power by making contracts about them."81 Suppose, for example, that a debtor and one of his unsecured creditors signed a contract providing that in the event of insolvency the claim of that particular creditor would be paid before those of all other creditors. If the debtor went bankrupt and the creditor came into bankruptcy court to enforce this contract, he would be met with hearty laughter; if he claimed that failure to enforce

his agreement would violate the Constitution, the laughter would only increase. One simply cannot contract out of the bankruptcy power.

3. The Requirement of Preservation of the Value of Collateral. — Even if the supposed distinction between secured creditors’ "property" rights and unsecured creditors’ “contractual” claims provided a persuasive reason for distinguishing between the constitutional rights of secured creditors and those of unsecured creditors, that distinction would fail to explain the assumption of the Unconstitutional Impairment Thesis that preservation of the value of the collateral is the key constitutional right of the secured creditor. One who contends that secured creditors’ “property” rights are entitled to special constitutional protection might argue that the secured creditor should be protected against any impairment of the rights that he would otherwise enjoy by virtue of his state-created property rights in the collateral. It is, however, quite clear that our present reorganization system does not provide such extensive protection. Yet once one concedes that such full protection is not compelled, one is left without any principled basis for asserting that a specific lesser degree of protection — preservation of the value of the collateral — is required.

Although commentators have occasionally asserted that Congress cannot, without granting compensation, authorize any action in reorganization proceedings that might place the secured creditor in an economic position less advantageous than the position he would occupy if his collateral were liquidated at the date of the inception of bankruptcy proceedings,82 our bankruptcy system falls far short of this level of protection. Consider the problems presented when the value of the secured creditor’s collateral is at least equal to the principal amount of the debt but prevailing rates of interest have risen since the time the loan was made. If the secured creditor were not restrained from exercising his contractual rights, he could have the property sold at a judicial sale, obtain full repayment of his loan, and reinvest the proceeds at prevailing interest rates. If the constitutional requirement in reorganization proceedings were that the secured creditor’s economic position not be impaired, restraint of foreclosure would be permissible only if interest accrued during the reorganization at prevailing market rates, not the contract rate; furthermore, the restraint could be continued only as long as the value of the property exceeded the amount of the debt plus interest at prevailing market rates. Our present reorganization

82 Chicago Comment, supra note 7, at 517.
system hardly guarantees the secured creditor such treatment. 83

Indeed, even aside from the matter of fluctuation in prevailing interest rates, our reorganization practice is not consistent with the thesis that a secured creditor's economic position may not be impaired. Suppose, for example, that at the inception of reorganization proceedings the value of the secured creditor's collateral were exactly equal to the principal amount of his claim. Even if the value of the collateral did not depreciate, a requirement of full protection of the secured creditor's economic position would preclude any restraint of foreclosure, for as time passes the secured creditor's economic position will be eroded by the increasing inability of the collateral to cover the amount of the debt plus accrued interest. 84 Yet the adequate protection provisions of the new Bankruptcy Code require only that the secured creditor be protected against any decrease in the value of his interest in the collateral, 85 and hence do not preclude impairment of the secured party's total economic position resulting from the inability of the collateral to cover accrued interest. 86

Thus, the supposed constitutional requirement of protection of the value of the secured creditor's collateral, as mirrored in the statutory adequate protection provisions, falls far short of protecting the economic position that the secured creditor sought by obtaining collateral and would have enjoyed had bankruptcy proceedings not been initiated. 87 There is, how-

83 There are significant limits on the accrual of postpetition interest even at the contract rate, see infra note 84, and I have never even seen it argued that a creditor could claim interest at a higher market rate. Cf. 4 COLLIER, supra note 7, § 542.03, at 542-7 to -8 & n.1 (secured creditor who is required to turn over property to the trustee under Bankruptcy Code § 542, 11 U.S.C. § 542 (Supp. V 1981), is not entitled to adequate protection for forgone profits from his own alternative use of the property).

84 Although the old Bankruptcy Act was silent on the issue of the accrual of interest, it seems to have been generally accepted that a secured creditor is entitled to claim postpetition interest in addition to principal only up to a maximum fixed by the value of his collateral. See In re Penn Cent. Transp. Co., 454 F.2d 9, 16 (3d Cir. 1972); 6 COLLIER ON BANKRUPTCY § 9.08 (J. Moore 14th ed. 1978). These principles have been codified in § 506(b) of the new Bankruptcy Code, 11 U.S.C. § 506(b) (Supp. V 1981).


86 For an extensive consideration of the issue of adequate protection of postpetition interest, reaching the same conclusion expressed in the text, see O'Toole, Adequate Protection and Postpetition Interest in Chapter 11 Proceedings, 56 AM. BANKR. L.J. 251 (1982).

87 In another sense, however, the notion that the value of the collateral is the measure of secured creditors' constitutionally protected rights might be thought overly generous. In the first place, a secured creditor who sustains a loss as a result of a stay of foreclosure in an unsuccessful reorganization will receive a federal income tax
ever, no apparent explanation for the assumption that the less rigorous requirement of preservation of the value of collateral marks a bright line beyond which impairment of the secured creditor's economic position becomes impermissible. Indeed, the relationship between the secured creditor's total economic interest and the value of the collateral is wholly fortuitous: it depends entirely on such factors as the contract interest rate, the prevailing market interest rate, and the duration of the reorganization proceedings.

Thus, even if one could find a commodious textual or jurisprudential mooring for the notion that fifth amendment principles limit even prospective bankruptcy legislation, one would encounter serious problems in attempting to support the Unconstitutional Impairment Thesis; it is very difficult to find any principled basis for either the Thesis' sharp distinction between the rights of secured and unsecured creditors or the Thesis' emphasis on the preservation of the value of collateral as the matter of critical constitutional significance. Moreover, these problems equally cast doubt on even a limited version of the Thesis — that secured creditors' rights to have the value of their collateral preserved may not constitutionally be impaired by retroactive bankruptcy legislation. This matter is discussed in more detail in Part III of this Article.

II. THE RELATIONSHIP BETWEEN THE FIFTH AMENDMENT AND THE BANKRUPTCY CLAUSE

The preceding Part demonstrates that the Unconstitutional Impairment Thesis is wholly unsatisfactory. I submit that the fundamental flaw in the Thesis is the assumption that the takings clause or other fifth amendment principles provide an independent source of limitations on the substantive scope of the bankruptcy power. In the balance of this Article, I develop an alternative view of the relationship between the bankruptcy clause and the family of constitutional provisions — including the takings clause, the due process clause, and the contracts clause — that limit the extent to which contractual or property
deduction for the amount of his loss. See Rosenberg, supra note 7, at 538-39. The federal government thus already provides a form of partial compensation for the losses that may be inflicted by the reorganization system. Furthermore, one might contend that no creditor can be constitutionally entitled to more than repayment of his loan in full plus a fair interest rate for the period during which the loan was outstanding. If a secured creditor has been charging a premium above the risk-free lending rate to protect himself against the possibility of nonpayment, one might argue that the added interest that he has received during the term of the loan must be deducted from the amount to which he is entitled.
Rights may be impaired by governmental action. My thesis is that these constitutional provisions do not impose substantive limitations on congressional exercise of the bankruptcy power. Instead, the principal source of substantive limitations on bankruptcy legislation is the bankruptcy clause itself, and hence the constitutionality of a statute adopted under the bankruptcy clause depends only on whether the measure falls within the scope of the powers conferred by the bankruptcy clause.

In this Part, I examine the principal nineteenth and early twentieth century decisions that resolved the fundamental issues concerning the constitutionality of bankruptcy legislation, and demonstrate that these decisions support the model of the relationship between the bankruptcy clause and the fifth amendment described above rather than the model implicit in the Unconstitutional Impairment Thesis. Moreover, in the course of examining the development of bankruptcy legislation, I attempt to define the scope of the bankruptcy power as it has evolved during the past two centuries. Finally, I consider the constitutionality of restraint of secured creditors' rights in reorganization from the perspective of this model.

A. The Historical Development of the Scope of the Bankruptcy Power

The first step in a satisfactory analysis of the constitutional limits of the bankruptcy power is to consider why the fifth amendment, or analogous constitutional principles, has not been regarded as a significant restraint on the extent to which bankruptcy law may impair unsecured creditors' rights. Careful examination of the nineteenth century cases that resolved basic issues concerning the constitutionality of bankruptcy legislation reveals that the courts did not rely on any simplistic notion of the supposed distinction between contractual and property rights. Rather, the substantial impairments of unsecured creditors' rights that are effected by any bankruptcy legislation were upheld against constitutional challenge on the ground that, because such impairments are inevitable in the bankruptcy system, they necessarily must be authorized by the bankruptcy clause.

1. Scope of the Bankruptcy Power: Voluntary Straight Bankruptcy. — The first significant case in the evolution of the analysis of the relationship between the bankruptcy clause and the fifth amendment is *In re Klein*, which involved the

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88 14 F. Cas. 716 (C.C.D. Mo.) (No. 7865), rev'd 14 F. Cas. 719 (D. Mo. 1843) (No. 7866).
1841 Bankruptcy Act. The 1841 Act, in a sharp departure from prior English bankruptcy law and the 1800 federal bankruptcy act, was at least as much a measure for the relief of debtors as it was a creditors' remedy: it provided for voluntary bankruptcies; it applied to any type of debtor rather than being limited to those engaged in trade; and it provided for the discharge of debts without the consent of creditors.

In the district court, Judge Wells held the 1841 Act unconstitutional, essentially on the theory that the power conferred on Congress by the bankruptcy clause was only the power to enact bankruptcy legislation substantially as it had been known in English law at the time the Constitution was adopted.

The district court's ruling in *In re Klein* was reversed on appeal in an opinion written by Justice Catron of the Supreme Court, sitting on circuit. Justice Catron rejected the district court's approach of tying the bankruptcy power to prior English practice, and adopted an expansive view of the power conferred by the bankruptcy clause:

> I hold [that the bankruptcy power] extends to all cases where the law causes to be distributed the property of the debtor among his creditors; this is its least limit. Its greatest is a discharge of the debtor from his contracts. And all intermediate legislation, affecting substance and form, but tending to further the great end of the subject — distribution and discharge — are in the competency and discretion of congress. With the policy of a law, letting in all classes, others as well as traders, and permitting the bankrupt to come in voluntarily, and be discharged without the consent of his creditors, the courts have no concern; it belongs to the law makers.

The difference between the approaches of Judge Wells and Justice Catron is quite significant. Judge Wells' opinion rests on alternative grounds: first, that English practice defined the

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92 See C. Warren, BANKRUPTCY IN UNITED STATES HISTORY 49–92 (1935).
93 See 1 H. Remington, supra note 90, § 8.
94 14 F. Cas. 719 (D. Mo.) (No. 7866), rev'd, 14 F. Cas. 716 (C.C.D. Mo. 1843) (No. 7865).
95 See id. at 720–21.
96 14 F. Cas. 716 (C.C.D. Mo. 1843) (No. 7865).
97 Id. at 718.
scope of the bankruptcy power and confined it to creditors' relief measures,\(^{98}\) and second, that the 1841 Act violated the contracts clause.\(^{99}\) It is the latter argument that is of interest here. Judge Wells regarded the principles embodied in the contracts clause as fundamental limits on the power of government that must apply to the federal government as well as to the states,\(^{100}\) and he seems to have considered it obvious that a statute that permits a debtor to initiate a voluntary bankruptcy proceeding and obtain a discharge of his debts is a law impairing the obligation of contracts.\(^{101}\) Thus, Judge Wells' opinion may be interpreted to suggest that creditors' rights to have the debtor's property devoted to satisfaction of their claims are entitled to constitutional protection and that the necessity of protecting such rights operates as an independent limitation on the permissible exercise of the bankruptcy power.

Justice Catron's expansive view of the bankruptcy power cannot be fit within such a model. Justice Catron did not dispute Judge Wells' suggestion that creditors' rights might in some contexts be entitled to constitutional protection. Rather, Justice Catron's response to Judge Wells' contracts clause argument was simply that the bankruptcy clause confers on Congress the authority to enact legislation that has the effect of impairing the obligation of contracts.\(^{102}\) Under Justice Catron's approach, the contracts clause component of the fifth amendment has no independent significance in the context of bankruptcy legislation. Instead, Justice Catron's view seems to have been that, if the act in question falls within the scope of the bankruptcy power, no question of unconstitutional impairment of the obligation of contracts is presented. Though the Klein decision was not appealed to the Supreme Court, its authority is beyond question; indeed, Justice Catron's opinion

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\(^{98}\) See 14 F. Cas. at 720-21.

\(^{99}\) See id. at 722-27.

\(^{100}\) Id. at 724-25 (contracts clause contains "a great principle of justice, which no legislative body should violate"). Judge Wells presented two arguments to explain the absence of a constitutional provision explicitly barring federal laws impairing the obligation of contracts. First, he suggested that such a provision would have been unnecessary, because the federal government possesses only those powers explicitly conferred by the Constitution, none of which includes the power to impair the obligation of contracts. Id. at 725. Second, he suggested that the takings clause of the fifth amendment may be read to encompass contracts clause principles. Id. at 729.

\(^{101}\) Id. at 722-23.

\(^{102}\) 14 F. Cas. at 717-18.
has been cited frequently by the Court as the leading statement of the scope of the bankruptcy power.\textsuperscript{103} 

The approval in \textit{Klein} of legislation providing for voluntary straight bankruptcy marks the beginning of the evolution of the modern concept of bankruptcy. At any given time, a debtor owns a certain pool of economic values that might be devoted to the repayment of his debts. Viewed broadly, the debtor's pool of economic values would include not only his existing assets, but also his earning power, from which the debtor may derive additional property in the future. Although the complexities of the early common law system for the collection of money judgments enabled creditors to reach only certain types of the debtor's assets, by at least the middle of the nineteenth century essentially all of the debtor's pool of economic values could be reached to satisfy the demands of creditors, except to the extent of limitation by exemption laws and doctrines of dormancy.\textsuperscript{104}

A bankruptcy act that permits a debtor to initiate voluntary bankruptcy and obtain a discharge significantly limits the extent to which the debtor's pool of economic values may be devoted to the satisfaction of claims of creditors. The discharge provisions\textsuperscript{105} effectively exempt the debtor's earning power from the reach of his creditors, and the exemption provisions\textsuperscript{106} remove a certain portion of the debtor's existing property from the reach of creditors. The justification for these limitations is, of course, the familiar "fresh start" policy of bankruptcy law.\textsuperscript{107} The early cases such as \textit{In re Klein} determined that exemption and discharge provisions were generally constitutional. Therefore, the substantive power conferred by the bankruptcy clause includes at least the authority to determine the extent to which a debtor's pool of economic values shall be devoted to the satisfaction of the claims of his existing creditors.

\textbf{2. Scope of the Bankruptcy Power: Binding Compositions.} — The next significant step in the evolution of the bankruptcy power came in 1874 when Congress, for the first time, adopted


\textsuperscript{104} See \textit{Riesenfeld, Collection of Money Judgments in American Law — A Historical Inventory and a Prospectus}, 42 \textit{Iowa L. Rev.} 155 (1957).


\textsuperscript{106} \textit{Id.} § 522, 11 U.S.C. § 522.

\textsuperscript{107} \textit{See}, e.g., \textit{Local Loan Co. v. Hunt}, 292 U.S. 234, 244 (1934).
a bankruptcy provision permitting a composition arrangement accepted by a majority of creditors to bind dissenting creditors. In the case of In re Reiman, the constitutionality of the 1874 Act was challenged by creditors who had dissented from a composition approved by the necessary majority of the creditors of two partners engaged in a business enterprise. The report of the case does not indicate whether the dissenting creditors explicitly relied upon the fifth amendment. It does, however, state that the dissenting creditors contended that the release of a debtor from his debts must be accompanied by a surrender of all of his property to his creditors and that a "law which provides for such release, without such surrender, is, so far as non-assenting creditors are concerned, merely a law for the confiscation of their debts, for the benefit of the bankrupt or debtor, and not a law on the subject of bankruptcies, within the meaning of the constitution."  

The Act was upheld in In re Reiman, and both the district and circuit courts, following Justice Catron's approach in In re Klein, devoted their opinions entirely to the question whether the Act fell within the scope of the powers conferred by the bankruptcy clause. The opinions contain no suggestion that the fifth amendment operates as an independent limitation on the scope of the bankruptcy power.  

In re Reiman's approval of the principle of binding compositions marks a significant step in the evolution of the concept of bankruptcy, for the composition principle lies at the heart of the reorganization provisions of modern bankruptcy law. In one sense, composition proceedings differ only slightly from straight bankruptcy proceedings. Both types of proceedings can be described as procedures implementing governmental decisions concerning the extent to which a debtor's pool of economic values shall be devoted to the satisfaction of his creditors' claims: in straight bankruptcy the debtor's future earning power is freed from the demands of creditors, leaving them to seek repayment out of the debtor's existing nonexempt

108 Act of June 22, 1874, ch. 390, § 17, 18 Stat. 178, 182. For the history of the 1874 provision, see C. Warren, supra note 92, at 118-20. A composition provision had been included in an 1827 bankruptcy bill that was not enacted. Id. at 44-45.

109 20 F. Cas. 490 (S.D.N.Y. 1874) (No. 11,673), aff'd, 20 F. Cas. 500 (C.C.S.D.N.Y. 1875) (No. 11,675).

110 Id. at 493.

111 In re Reiman was not appealed to the Supreme Court, but later Supreme Court cases adopted and approved the analysis of the Reiman decision. See, e.g., Continental Ill. Nat'l Bank & Trust Co. v. Chicago, R.I. & Pac. Ry. (Rock Island), 294 U.S. 648, 672-73 (1935); Hanover Nat'l Bank v. Moyses, 186 U.S. 181, 186 (1902).
assets; in composition proceedings the debtor's existing assets are freed from the demands of creditors, leaving them to seek repayment only from the debtor's future earnings. One might suggest, therefore, that the approval of the composition principle in *Reiman* represents only a limited development from the *Klein* concept of bankruptcy as simply a matter of limiting the extent to which the debtor's pool of economic values shall be devoted to the satisfaction of his creditors' claims. Subsequent cases, however, make clear that far more is involved in the acceptance of the composition principle.

3. Scope of the Bankruptcy Power: Reorganization. — The significance of the composition concept is suggested by the Supreme Court's decision in the 1883 case of *Canada Southern Railway v. Gebhard*. Holders of mortgage bonds of a Canadian railway corporation brought suit on their bonds in a United States circuit court. The railroad defended on the basis of an act of the Canadian Parliament that bound non-asserting creditors, such as the plaintiffs, to the terms of an arrangement approved by a majority of the creditors of the railroad. The Supreme Court's opinion accepting the railroad's defense may have been based solely on the view that the arrangement was valid under Canadian law, but the opinion also suggests that the arrangement would have been entirely proper even if tested under the standards of the United States Constitution:

The confirmation and legalization of "a scheme of arrangement" under such circumstances is no more than is done in bankruptcy when a "composition" agreement with the bankrupt debtor, if assented to by the required majority of creditors, is made binding on the non-asserting minority. In no just sense do such governmental regulations deprive a person of his property without due process of law. They simply require each individual to so conduct himself for the general good as not unnecessarily to injure another. Bankrupt laws have been in force in England for more than three centuries, and they had their origin in the Roman law. The Constitution expressly empowers the Congress of the United States to establish such laws. Every member of a political community must necessarily part with some of the rights which, as an individual, not affected by his relation to others, he might have retained. Such concessions make up the consideration he gives for the obligation of the body politic to protect him

112 109 U.S. 527 (1883).
113 See id. at 528, 531.
114 See id. at 529–32.
115 See id. at 536–40.
in life, liberty, and property. Bankrupt laws, whatever may be the form they assume, are of that character.\footnote{Id. at 536; accord id. at 539.}

Any question about the force of what may have been dicta in \textit{Canada Southern} was laid to rest in \textit{Continental Illinois National Bank & Trust Co. v. Chicago, Rock Island and Pacific Ry.}\footnote{294 U.S. 648 (1935).} \textit{Rock Island} was the Supreme Court's first decision on the constitutionality of a modern reorganization act, the railroad reorganization provisions of section 77 of the Bankruptcy Act.\footnote{Act of Mar. 3, 1933, ch. 8, § 77, 47 Stat. 1467, 1474 (current version at Bankruptcy Code §§ 1161–1174, 11 U.S.C. §§ 1161–1174 (Supp. V 1981)).} Justice Sutherland's opinion traced the development of bankruptcy legislation and noted that each extension of the concept of bankruptcy had been held constitutional.\footnote{See 294 U.S. at 667–71.} As to the reorganization concept embodied in section 77, the Court held that the approval of the composition principle in \textit{In re Reiman} and \textit{Canada Southern} sufficed to demonstrate that section 77 fell within the scope of the bankruptcy power.\footnote{Id. at 671–75.} The Court quoted and explicitly approved the \textit{Canada Southern} discussion of the relationship between the bankruptcy power and the due process clause.\footnote{Id. at 673–75.}

The \textit{Canada Southern} and \textit{Rock Island} cases are significant at two levels. First, \textit{Klein} and \textit{Reiman} involved challenges to bankruptcy legislation brought by unsecured creditors; hence adherents of the Unconstitutional Impairment Thesis might, on that ground, consider the two cases to be beside the point. \textit{Canada Southern} and \textit{Rock Island}, however, involved challenges brought by secured creditors. Nonetheless, the constitutional analysis applied was that developed in \textit{Klein} and the other nineteenth century cases dealing with unsecured creditors' rights. Indeed, in \textit{Canada Southern} the Court explicitly referred to the due process clause and made it quite clear that a valid exercise of the bankruptcy power is not open to attack on fifth amendment grounds.\footnote{109 U.S. at 536. The impairment of the rights of the secured creditors in \textit{Canada Southern} was by no means insubstantial. Indeed, the arrangement imposed by act of the Canadian Parliament did not even comply with the absolute priority rule: the claims of holders of mortgage bonds for accrued interest were extinguished even though holders of junior mortgage bonds and stockholders retained interests in the reorganized company. Id. at 530.}

Second, the approval of bankruptcy legislation providing for reorganization of corporate enterprises represents a signif-
icant advance in the evolution of the bankruptcy power. In the case of individual debtors, such as the partners in *In re Reiman*, the composition concept might be viewed as simply an alternative method of distributing to creditors the portion of the debtor's pool of economic values that is not essential to his fresh start. Yet because the fresh start policy of straight bankruptcy is in large measure a humanitarian concept applicable only to individual debtors, the application of the composition concept to corporate debtors must rest squarely on the proposition that preserving the earning power of an existing enterprise for the benefit of all those affected by its affairs is a legitimate objective of bankruptcy legislation. Moreover, in the case of business enterprises, there is a close relationship between the use of existing assets and future earning power. A natural person's future earning power may be largely a function of his intelligence, skill, industry, and other personal characteristics, but the future earning power of a business enterprise is in large part a function of the uses to which its assets are devoted. Accordingly, preserving the earning power of a business enterprise invariably requires assertion of control over the use of the enterprise's existing assets — for example, as in *In re Reiman*, by abrogating creditors' rights to have those assets immediately devoted to the satisfaction of the creditors' claims. Thus, *In re Reiman, Canada Southern*, and *Rock Island* suggest an expansion of the scope of the substantive powers conferred by the bankruptcy clause: the bankruptcy clause confers on the federal government the authority to exercise control over the use of the debtor's existing assets in order to enhance and preserve his earning power.\(^\text{123}\)

**B. The Permissibility of Restraint of Secured Creditors' Foreclosure Rights**

Thus far, I have considered at a general level the analysis of the relationship between the bankruptcy clause and the fifth amendment that was developed and applied in the nineteenth and early twentieth century bankruptcy cases. In this Section,

\(^{123}\) Indeed, the proposition that the bankruptcy power comprehends the power to take action intended to preserve the debtor's earning power may be implicit even in simple bankruptcy legislation of the sort involved in *In re Klein*. The fresh start policy may, in part, be seen as a reflection of the fear that permitting creditors to exercise fully their state law collection rights might destroy the debtor's earning power. Saddled with debts, deprived of assets necessary for minimal comfort, and knowing that the fruits of his endeavors will be taken by creditors, the debtor may simply forgo productive activity, and economic society will lose a potentially productive member.
I use the proposition that the limits on the substantive scope of the bankruptcy power derive from the bankruptcy clause itself to examine the extent to which secured creditors may be restrained from foreclosing on their collateral during the pendency of reorganization proceedings.

The issue of the permissibility of interim stays of secured creditors' foreclosure rights was considered by the Supreme Court in the *Rock Island* case, in which the reorganization court had entered an order restraining a group of secured creditors of the railroad from selling or disposing of their collateral pending the effort to devise a plan of reorganization. It is quite noteworthy that, before addressing the secured creditors' contention that the restraint order violated the fifth amendment, the Supreme Court felt it necessary to consider the constitutionality of the railroad reorganization act in general as an exercise of the bankruptcy power, even though that issue had not been raised by the parties. This approach is precisely what one would expect of a court applying the model of constitutional analysis developed in *In re Klein* and the other nineteenth century cases. Having found that the pursuit of reorganization was a legitimate objective of bankruptcy legislation, the Court readily concluded that the reorganization court had authority to enjoin secured creditors from selling the collateral "if a sale would so hinder, obstruct and delay the preparation and consummation of a plan of reorganization as probably to prevent it." Moreover, as one would expect in light of the constitutional model developed in the nineteenth century cases, when the Court passed from consideration of the constitutionality of section 77 under the bankruptcy clause to the fifth amendment challenge, it found the latter issue entirely unproblematic. Justice Sutherland's remarks are worth setting forth at length:

We find no substance in the contention of the petitioning banks that § 77, as applied by the court below to permit an injunction restraining the sale of the collateral, violates the Fifth Amendment. The basis of the contention is that since, by the terms of the pledge, the pledgors are empowered on default to sell the collateral at such times as they may select, § 77, as thus applied, deprives them of their property — that is to say, impairs or destroys their contractual rights — without due process of law.

The Constitution, as it many times has been pointed out, does not in terms prohibit Congress from impairing the obli—

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124 See 294 U.S. at 656-61.
125 See id. at 667; supra p. 1004.
126 294 U.S. at 675.
igation of contracts as it does the states. But as far back as
_Calder v. Bull_, 3 Dall. 386, 388, it was said that among other
acts which Congress could not pass without exceeding its
authority was "a law that destroys or impairs the lawful
private contracts of citizens." The broad reach of that state-
ment has been restricted; but the principle which it includes
has never been repudiated, although the extent to which it
may be carried has not been definitely fixed. Speaking gen-
erally, it may be said that Congress, while without power to
impair the obligation of contracts by laws acting directly and
independently to that end, undeniably, has authority to pass
legislation pertinent to any of the powers conferred by the
Constitution, however it may operate collaterally or inciden-
tally to impair or destroy the obligation of private contracts.
And under the express power to pass uniform laws on the
subject of bankruptcies, the legislation is valid though drawn
with the direct aim and effect of relieving insolvent persons
in whole or in part from the payment of their debts. So much
necessarily results from the nature of the power, and this must
have been within the contemplation of the framers of the
Constitution when the power was granted.127

This passage is about as clear a statement of the relationship
between the fifth amendment and the bankruptcy clause as
can be found in the case law.

The significance of _Rock Island_ is highlighted by the strik-
ing contrast between that decision and _Home Building & Loan
Association v. Blaisdell_,128 decided one year before _Rock Is-
land_. In _Blaisdell_, a contracts clause and due process129 chal-
lenege to the Minnestota Mortgage Moratorium Act, which
authorized a stay of foreclosure for no more than two years,130
was rejected by only a five-to-four decision and over the
strongly worded dissent of Justice Sutherland.131 By the time
the Supreme Court rendered its decision in _Rock Island_, the
secured creditors in that case had already been restrained for
a period of sixteen months,132 yet it was Justice Sutherland,
writing for a unanimous Court, who readily upheld the order
enjoining the secured creditors from foreclosing. The differ-

127 Id. at 680–81 (citations omitted).
128 290 U.S. 398 (1934).
129 Although _Blaisdell_ is generally regarded as a contracts clause case, the mort-
gagee also contended that the challenged statute took his property without due process
of law, id. at 404. Chief Justice Hughes' opinion for the majority appears to consider
the two contentions essentially equivalent. See id. at 448.
130 See id. at 415–16 (discussing Act of Apr. 18, 1933, 1933 Minn. Laws ch. 339).
131 See id. at 448–53 (Sutherland, J., dissenting).
132 See _Rock Island_, 294 U.S. at 648, 657.
ence between the two cases is only that the federal government possesses a power denied to the states — the bankruptcy power. Thus, the only explanation for the striking difference between the Court's responses in the two cases is the proposition that the bankruptcy clause trumps the fifth amendment.

The Rock Island case thus suggests that questions concerning the constitutionality of interim restraints of secured creditors' foreclosure rights should be analyzed in the same manner as is any other issue involving the constitutionality of bankruptcy legislation — solely as a matter of the substantive scope of the bankruptcy power. As an illustration of such analysis, consider the issues posed by the much-discussed Yale Express case. The district court denied both the secured creditor's petition for leave to reclaim collateral pursuant to its security agreement and the secured creditor's request for rental payments to compensate it for depreciation of the collateral. The Second Circuit affirmed the denial of the secured creditor's petitions, on the grounds that use of the equipment was essential to continuation of the business and that there was a reasonable probability of successful reorganization. Although the Yale Express opinions did not discuss constitutional issues, some commentators have suggested that the impairment of the secured creditor's rights in Yale Express raises serious constitutional questions under the fifth amendment.

The only difference between Rock Island and Yale Express is that in Yale Express it was quite certain that the secured creditor's specific collateral would depreciate during the course of the proceedings. Nonetheless, the secured creditor in Yale Express faced a risk of loss only if the reorganization court's prediction of the likelihood of successful reorganization proved to be incorrect. Thus, the assertion of a secured creditor that he cannot be subjected to the risk of unsuccessful reorganization is, in essence, an assertion that he has the right to require that the prospect of salvaging going concern values be

133 In re Yale Express Sys., 384 F.2d 990 (2d Cir. 1967).
134 See id. at 991–92.
135 Id.
136 See Murphy I, supra note 7, at 34, 45–46; Rosenberg, supra note 7, at 525–31; N.Y.U. Note, supra note 7, at 392 n.203.
137 Indeed, in Yale Express, the secured creditor faced a risk of loss only if the effort to reorganize failed and there were no other assets available for payment of the creditor's priority unsecured claim for the amount of depreciation of the collateral. See infra pp. 1028–29.

In fact, the Yale Express reorganization was successful. The plan of reorganization provided for the satisfaction of all creditors' claims, including postpetition interest, and some participation for stockholders was confirmed. See In re Yale Express Sys., 366 F. Supp. 1376, 1380 & n.2 (S.D.N.Y. 1973).
sacrificed to ensure absolute protection of his interests. Yet in light of the delineation of the scope of the bankruptcy power in In re Reiman, Canada Southern, and Rock Island, it is quite clear that exercising control over the debtor's existing assets in an effort to preserve the earning power of the debtor is a permissible exercise of the bankruptcy power and hence, on that ground alone, is not vulnerable to fifth amendment challenge.

The possibility that the reorganization system may err in its prediction of the likelihood of successful reorganization does not preclude the exercise of the power to attempt reorganizations. For example, in In re Reiman it was explicitly ruled that the 1874 Act authorized a composition in which creditors received notes rather than cash.\textsuperscript{138} Nothing in the opinions suggests that it occurred to the courts or to any of the parties that the inevitable risk of nonpayment of the notes and further deterioration of the debtor's financial position raised any constitutional problems.\textsuperscript{139} Similarly, nothing in the Canada Southern opinion suggests any judicial concern with the possibility that the creditors might suffer loss by being forced to accept securities in the reorganized enterprise rather than being permitted to enforce their prior claims against the property of the debtor. The only mention of the problem in Rock Island comes in a passage in which the Court noted that the value of the collateral might decline during the period of the stay, but suggested that such problems raise only a question for the reorganization court to consider in the exercise of its discretion in ruling on requests for stays or relief therefrom.\textsuperscript{140} Such

\begin{itemize}
\item \textsuperscript{138} 20 F. Cas. at 502; 20 F. Cas. at 497–498.
\item \textsuperscript{139} The debtor, of course, would not obtain his discharge if he failed to pay the notes. In re Reiman, 20 F. Cas. 490, 497–498 (S.D.N.Y. 1874) (No. 11,673), aff'd, 20 F. Cas. 500 (C.C.S.D.N.Y. 1875) (No. 11,675). The point, however, is that the value of the debtor's property might decline during the period in which composition payments were being made.
\item \textsuperscript{140} 294 U.S. at 677. The Rock Island case is sometimes said to have posed a fairly easy problem, on the ground that the value of the collateral held by the secured parties far exceeded the amount of the debt secured. See Chicago Comment, supra note 7, at 513–15; Yale Note I, supra note 7, at 1611–12. Had that been the case, there would have been little risk that the creditors' position would have been impaired by the stay. It is not so clear, however, that this was the case. The creditors objecting to the stay were holders of collateral trust bonds aggregating $17,784,877.\textsuperscript{58}. See 294 U.S. at 657–60. The collateral for this claim consisted of other mortgage bonds of the Rock Island and its subsidiaries in the face amount of $56,111,465.\textsuperscript{55}. Id. The face amount of the subsidiary mortgage bonds, however, can hardly be taken as the value of the collateral securing the collateral trust bonds, see A. Dewing, The Financial Policy of Corporations 210–14 (5th ed. 1953), and there is no discussion in the opinion of the value of the property securing the subsidiary mortgage bonds.
\end{itemize}
language is hardly what one would expect if preservation of the value of collateral represented a rigid limitation on the constitutionality of exercises of the bankruptcy power.

Some commentators have suggested that the Supreme Court’s 1974 decision in the Regional Rail Reorganization Act Cases (RRRA Cases)\(^\text{141}\) provides substantial support for the view that fifth amendment concepts concerning the protection of secured creditors’ property rights impose limitations on the permissible extent of interim restraints of secured creditors’ rights during reorganization proceedings.\(^\text{142}\) The Penn Central Railroad entered reorganization proceedings in 1970.\(^\text{143}\) In 1974, Congress enacted the Regional Rail Reorganization Act (RRRA),\(^\text{144}\) which provided that the rail properties of the Penn Central and of certain other northeastern railroads also in reorganization would be conveyed to a private state-incorporated corporation, Consolidated Rail Corporation (Conrail). In return, the estates of the debtor railroads were to receive Conrail securities and obligations of a government corporation, the United States Railway Association, which were guaranteed by the United States.\(^\text{145}\) Various creditors of Penn Central filed suit contending that the RRRA violated the takings clause, in part on the theory that the Act’s requirement of continued rail operations pending the conveyance would erode the value of the Penn Central estate.\(^\text{146}\) In the RRRA Cases, the Supreme Court sidestepped the takings clause issues by concluding that the Act did not displace remedies that would otherwise be available to the Penn Central estate under the Tucker Act;\(^\text{147}\) thus, if the RRRA failed to afford the Penn Central estate constitutionally adequate compensation, the estate could sue the United States in the Court of Claims under the Tucker Act to obtain just compensation.\(^\text{148}\)


\(^\text{142}\) See, e.g., N.Y.U. Note, supra note 7, at 391 n.203, 399–401.

\(^\text{143}\) See RRRA Cases, 419 U.S. at 117 n.12.


\(^\text{145}\) See RRRA Cases, 419 U.S. at 158–148.

\(^\text{146}\) See id. at 110.


\(^\text{148}\) See 419 U.S. at 125–36, 148. Congress subsequently amended the RRRA to take into account “compensable unconstitutional erosion” in compensating the estate. Railroad Reorganization and Regulatory Reform Act of 1976, Pub. L. No. 94-210, § 612(q), 90 Stat. 31, 114–12 (codified at 45 U.S.C. § 743(c) (1976)). It is unlikely that we shall see any definitive judicial resolution of the takings clause problems presented by the RRRA, because the valuation litigation has been settled, at least with respect to the principal parties. Wall St. J., Nov. 18, 1980, at 2, col. 2.
The suggestion that the *RRRA Cases* support the view that the fifth amendment limits the bankruptcy power does have a surface appeal. To be sure, the Supreme Court did not actually decide that the RRRA would violate the fifth amendment in the absence of compensation. Nonetheless, if the constitutional assertions had been insubstantial, it would have been a simple matter for the Court to say so, rather than undertake the heroic bit of statutory construction necessary to reach the conclusion that the Tucker Act remedy survived. In the *RRRA Cases*, however, it was irrelevant that the parties objecting to continued deficit operations happened to be secured creditors of an enterprise involved in reorganization proceedings. The issues presented would have been just the same if the claimants to the estate had consisted solely of holders of equity securities or even if the railroad had not been in reorganization proceedings. The issue was not whether one having the status of a secured creditor of a railroad has, by virtue of his secured status, a fifth amendment right to be free from erosion of the value of his particular collateral. Rather, the issue was whether investors in a railroad may be forced to accept an erosion of the value of the estate in its entirety caused by continued deficit operations.\(^{149}\)

The real problem in the Penn Central reorganization proceedings was that within a fairly short period after the reorganization proceedings were initiated it became apparent that a traditional reorganization simply was not possible;\(^ {150}\) the railroad had become a financial basket case. No one could

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\(^{149}\) Somewhat similar issues were presented in the New Haven Inclusion Cases, 399 U.S. 392 (1970), in which some of the New Haven Railroad's bondholders contended that a plan of reorganization proposed for the New Haven violated the requirements of the fifth amendment. They claimed that continued operation of the New Haven during the reorganization proceedings had resulted in an erosion of the estate by the accumulation of more than $70 million in administration expenses having priority over the bondholders' claims and that no compensation had been provided for this erosion. *Id.* at 489–90. As in the *RRRA Cases*, the constitutional problem was not that secured creditors enjoy some special constitutional immunity from the exercise of the bankruptcy power, but merely that the limits of the bankruptcy power may well have been exceeded, given that it was clear in the *New Haven* case, as in the *RRRA Cases*, that a traditional reorganization simply was not feasible. *See id.* at 404–07. The Supreme Court rejected the bondholders' fifth amendment contention, principally on procedural grounds. *See id.* at 493. There are indications in the opinion, however, that the bondholders' fifth amendment claims would have been rejected even in the absence of the above considerations, essentially on the ground that investors in a public utility such as a railroad, which has an obligation to serve the public, must be deemed to have accepted the risk that the value of their investment may be eroded in order that vital public services may be continued. *See id.* at 491–92.

\(^{150}\) *See RRRA Cases*, 419 U.S. at 123–24.
plausibly contend that the purpose of continued deficit operations was to maintain a going business in order to devise an effective plan of reorganization. Rather, the only reason for continuing operations was the public interest in continued rail service. In such a situation, legislation requiring continued operations to the detriment of the estate may well exceed the authority conferred by the bankruptcy clause.

Perhaps some source of substantive federal power aside from the bankruptcy clause authorizes legislation requiring the continued operation of railroads or other enterprises for the benefit of the public rather than for the benefit of the investors in the enterprise. Other sources of federal power that might authorize continued deficit operations may well not share the peculiar attribute of the bankruptcy power — its explicit authorization of the imposition of losses on private interests without compensation. Thus, although it is true that the RRRA Cases pose difficult takings clause issues, they do so not because the fifth amendment imposes substantive limitations on the bankruptcy power, but because the railroad cases may have presented situations beyond the reach of the bankruptcy power.

The contrast between Yale Express and the RRRA Cases illustrates the true relationship between the bankruptcy power and the fifth amendment. In any case involving an impairment of the rights of creditors or other investors in reorganization proceedings, the first issue is that of substantive power under the bankruptcy clause. If, as in Yale Express, the action in question is authorized under the bankruptcy clause, that determination will generally be the end of the matter as far as the fifth amendment goes. Only if, as in the RRRA Cases, the action in question cannot be justified under the bankruptcy power will a takings clause issue arise.

151 The principal issue would seem to be the question of the extent to which laws prohibiting the termination of public utility services without the approval of regulatory authorities place investors in such enterprises on notice that their investments may be impaired in the interest of preserving vital public services. See Yale Note II, supra note 7, at 387.

152 To be sure, Congress might elect to retain the adequate protection model as a method of protecting secured creditors to be employed when feasible. The analysis developed in this Article, however, demonstrates that nothing in the Constitution prevents Congress from authorizing the attempt to effect a reorganization in situations in which adequate protection cannot be provided. Congress might prefer to use the adequate protection technique, when feasible, on the ground that proof that secured creditors are adequately protected may be simpler than proof of the likelihood of reorganization. Cf. Rosenberg, supra note 7, at 525–32 (discussing difficulty of predicting likelihood of successful reorganization at inception of proceedings).
III. THE CONSTITUTIONALITY OF RETROACTIVE APPLICATION OF BANKRUPTCY LEGISLATION

Although the analysis developed thus far demonstrates that the fifth amendment does not significantly constrain the substantive scope of the bankruptcy power, it does not necessarily preclude the possibility that fifth amendment principles may limit the extent to which Congress can give retroactive application to amendments to bankruptcy legislation. The problem of retroactive bankruptcy legislation was recently considered by the Supreme Court in *United States v. Security Industrial Bank*. Relying on the canon of interpretation that statutes should be construed to avoid constitutional questions, the Court ruled that section 522(f) of the new Bankruptcy Code, which invalidates nonpossessory, non-purchase-money security interests in certain exempt property of the debtor, should be interpreted to apply only prospectively. Although *Security Industrial Bank* is less than a square holding on the constitutional issue, it warrants con-

153 It is true that in *Hanover Nat'l Bank v. Moyses*, 186 U.S. 181 (1902), the Supreme Court stated that “Congress may prescribe any regulations concerning discharge in bankruptcy that are not so grossly unreasonable as to be incompatible with fundamental law.” *Id.* at 192. It is not clear from this statement, however, whether the source of this rather trivial constraint on the exercise of the bankruptcy power is the fifth amendment due process clause or the bankruptcy clause. Exercise of the bankruptcy power is, of course, subject to certain fifth amendment constraints other than the general due process and takings provisions, such as the self-incrimination clause and the implied equal protection requirement.


156 103 S. Ct. at 412, 414. Justice Blackmun, joined by Justices Brennan and Marshall, wrote a separate opinion concurring in the judgment. *Id.* at 414 (Blackmun, J., concurring in the judgment). Justice Blackmun stated that, if he were to reach the constitutional issue, he would uphold the statute. *Id.* at 415. However, in light of *Holt v. Henley*, 232 U.S. 637 (1914), and *Auffm’ordt v. Rasin*, 102 U.S. 620 (1881), Justice Blackmun felt bound to rule, as a matter of statutory construction, that amendments to the bankruptcy legislation should if possible be construed to preserve rights. 103 S. Ct. at 415–16 (Blackmun, J., concurring in the judgment).

As Justice Blackmun’s opinion indicates, the result in *Security Industrial Bank* need not have rested on a finding that retroactive application of § 522(f) would raise substantial constitutional questions. Indeed, the cases on which both Justice Rehnquist and Justice Blackmun relied for the applicable canon of interpretation of bankruptcy law suggest that the presumption of prospective application is not dependent on any special constitutional rights of secured creditors. *Holt v. Henley* did involve a secured creditor’s contention that an amendment to the Bankruptcy Act should not be applied in a manner that would invalidate his lien, 232 U.S. at 639; in *Auffm’ordt*, however, the “vested right” in question was the right of the assignee in bankruptcy to invalidate a pledge as a preferential transfer notwithstanding a later amendment reducing the preference period.

157 See 103 S. Ct. at 410.
sideration as an indication of the Court's approach to retroactive bankruptcy legislation impairing secured creditors' rights. In this Part, the shortcomings of the Security Industrial Bank analysis are noted, and an alternative approach is suggested.\textsuperscript{158}

\textbf{A. The Inadequacy of the Security Industrial Bank Analysis}

In \textit{Security Industrial Bank}, Justice Rehnquist, writing for the majority, rejected the argument that retroactive application of bankruptcy legislation raises no constitutional problems as long as the measure in question is a rational exercise of the bankruptcy power. Justice Rehnquist conceded that the bankruptcy power authorizes retroactive impairments of contractual rights, but, relying solely on \textit{Radford}, he stated that, when exercise of the bankruptcy power impairs "traditional property interests," the question "whether the enactment takes property within the prohibition of the Fifth Amendment"\textsuperscript{159} is quite distinct from the question whether the act is a rational exercise of the bankruptcy power.

\textit{i. Comparison with Pre-Radford Analysis of Retroactive Bankruptcy Legislation.} — Although there is a surface appeal to the notion that bankruptcy legislation, like legislation on other subjects, may present more substantial constitutional problems if it is made retroactive rather than purely prospective, much in the case law suggests, contrary to Justice Rehnquist's position, that retroactivity is not an objectionable feature in bankruptcy legislation. Before the time of the \textit{Radford} decision, the federal courts had almost invariably approached questions concerning the constitutionality of bankruptcy leg-

\textsuperscript{158} If the Constitution significantly limits the extent to which Congress can retroactively apply amendments to bankruptcy legislation, that fact may substantially reduce the flexibility that the proper analysis of the relationship between the bankruptcy clause and the fifth amendment appears to give Congress in the design of bankruptcy policy. Debtors entering reorganization proceedings commonly have a variety of creditors who extended credit at varying times. In complex reorganizations, such as the Penn Central proceedings, the creditors may range from persons who extended trade credit days before the proceedings were commenced to holders of bonds issued in the nineteenth century. \textit{See In re Penn Cent. Transp. Co.}, 458 F. Supp. 1234 (E.D. Pa. 1978) (order approving plan), \textit{modified in part and aff'd}, 596 F.2d 1102, 1127, 1154 (3d Cir. 1979). A constitutional requirement that disputes concerning rights of creditors be resolved by reference to the law existing at the time each creditor extended credit might present intractable administrative problems that would inhibit adoption of even the entirely permissible prospective legislation. Some consideration of the limits of retroactive application of amendments to bankruptcy legislation is therefore a necessary complement to my analysis of the relationship between the bankruptcy clause and the fifth amendment.

\textsuperscript{159} 103 S. Ct. at 410.
islation exclusively in terms of the substantive scope of the bankruptcy power, and this analysis appears to have been regarded as an approach applicable to retroactive as well as prospective applications of the bankruptcy power and to cases involving secured creditors' rights as well as those involving unsecured creditors' rights. In fact, the cases from *In re Klein* through *Rock Island*, which were considered in Part II of this Article from the perspective of the source of constitutional limitations on the substantive scope of bankruptcy legislation, all appear to have involved retroactive application of newly enacted bankruptcy legislation. Moreover, the *Canada Southern* and *Rock Island* cases both involved retroactive impairments of secured creditors' "property" rights.

160 Aside from the circuit court decision in *In re Dillard*, 7 F. Cas. 703 (C.C.E.D. Va. 1873) (No. 3912), discussed at infra note 173, the only pre-Radford cases that I have found in which courts indicated that retroactivity might be a troublesome feature of bankruptcy legislation are several decisions that interpreted provisions of the bankruptcy law to be nonretroactive without discussing whether the Constitution would prohibit retroactive application. See *Holt v. Henley*, 232 U.S. 637 (1914); *Auffm'ordt v. Rasin*, 102 U.S. 620 (1881), discussed at supra note 156.

161 See supra pp. 998–1005.

162 The *Klein* case, decided in the district court in 1843, involved a challenge to the 1841 Bankruptcy Act, Act of Aug. 19, 1841, ch. 9, 5 Stat. 440, repealed by Act of Mar. 3, 1843, ch. 82g, 5 Stat. 614. The opinion does not state the date upon which the bankruptcy petition was filed or the dates upon which the debts were incurred; the opinion of the district court, however, explicitly states that the question under consideration was whether the 1841 Act could constitutionally be applied to debts contracted before the passage of the Act. 14 F. Cas. 719, 730 (D. Mo.) (No. 7866), rev'd, 14 F. Cas. 716 (C.C.D. Mo. 1843) (No. 7865). In *Canada Southern*, the mortgage bonds affected by the 1878 arrangement legislation were issued in 1871, 1873, and 1875. 109 U.S. at 528–29. In the *Rock Island* case, the railroad's § 77 petition was filed on June 7, 1933, 294 U.S. at 646, approximately three months after § 77 was enacted, see Act of Mar. 3, 1933, ch. 204, § 77, 47 Stat. 1467, 1474. The opinion of the court of appeals in *Rock Island* noted that the secured creditors who were challenging the Act had taken their pledges before the four-month preference period preceding the date of bankruptcy. Continental Ill. Nat'l Bank & Trust Co. v. Chicago, R.I. & Pac. Ry. (Rock Island), 72 F.2d 443, 449 (7th Cir. 1934), aff'd, 294 U.S. 648 (1935). Hence the creditors must have taken their pledges before the enactment of § 77.

The situation in the *Reiman* case is a bit less clear. The bankruptcy petition was filed on August 3, 1874, 20 F. Cas. 490, 490 (S.D.N.Y. 1874) (No. 11,073), aff'd, 20 F. Cas. 500 (C.C.S.D.N.Y. 1875) (No. 11,075), just six weeks after the 1867 Bankruptcy Act was amended by the Act of June 22, 1874, ch. 390, § 17, 18 Stat. 178, 182, which provided for composition proceedings. Although the date upon which the debts of the dissenting creditors were incurred is not specified, given that these creditors were owed some $30,000 out of the debtor's total debts of approximately $160,000, it seems plausible to suppose that their loans were not made in the six weeks before bankruptcy.

163 Furthermore, as has previously been discussed, see supra pp. 988–95, there is no sound theoretical basis for a distinction of constitutional dimension between the rights of secured creditors and those of unsecured creditors.
Yet in all of these cases, the constitutional issues were viewed solely as questions of the scope of the bankruptcy power.

The assumption that retroactive bankruptcy legislation poses constitutional issues separate from and more difficult than the issues of the substantive scope of the bankruptcy power may be a product of inattention to the history of bankruptcy legislation. Until the 1898 Act, bankruptcy legislation was not a permanent feature of federal law, but instead took the form of temporary relief measures adopted in response to specific financial crises and repealed when the precipitating cause had passed. As long as bankruptcy acts were seen as temporary relief measures enacted to alleviate existing economic troubles, the idea of nonretroactive bankruptcy legislation would be almost an absurdity: a newly enacted bankruptcy act that did not apply to preexisting debts could hardly relieve the plight of existing creditors or debtors. Thus, it is not surprising that retroactivity does not seem to have been viewed as a troublesome matter, or even a separate question, in the nineteenth and early twentieth century cases concerning the constitutionality of bankruptcy acts.

Even in the case of amendments to existing bankruptcy legislation, the nineteenth century cases do not appear to have regarded retroactivity as a question distinct from the issue of substantive bankruptcy power. Perhaps the most sharply focused challenge to bankruptcy legislation on the basis of retroactivity concepts involved the curious history of the exemption provisions of the 1867 Act. As originally enacted, the Act gave bankrupts the benefit of exemption laws in force in the state of their domicile in 1864. Just after the Civil War, many states greatly liberalized their exemption laws, but various state courts, and the United States Supreme Court,
held that it would violate the contracts clause for the states to apply their expanded exemption laws to debts incurred before the enactment of those laws.\textsuperscript{169} Despite the bar on action by the states, in 1872 Congress amended the 1867 Bankruptcy Act to give bankrupts the benefit of exemption laws in force in the state of their domicile in 1871.\textsuperscript{170} Congress adopted a further clarifying amendment in 1873\textsuperscript{171} to make explicit that bankrupts were to have the benefit of the exemption laws on the books in 1871 — even though those laws had been held invalid under the contracts clause as state legislation — and that such exemptions should be available even as against antecedent debts and even as against judicial liens previously acquired on the property.

Thus, the amendments to the 1867 Act provide a clear instance of a congressional exercise of the bankruptcy power that retroactively impaired the rights of creditors, including creditors holding judicial liens,\textsuperscript{172} in precisely the situation in which the Supreme Court had held that such retroactive legislation, when adopted by the states, violated the constitutional rights of creditors. Moreover, the situation was not one in which Congress enacted a bankruptcy statute and applied it to debts contracted at a time when no bankruptcy act was in force. Rather, it was a situation in which Congress sought to give retroactive force to an amendment to existing bankruptcy legislation in circumstances in which creditors might plausibly claim to have relied on the previous legislation. Nevertheless, although no case challenging the 1872 or 1873 amendments reached the Supreme Court, the decisions of the lower federal courts generally indicated that the retroactive feature of the amendments was not constitutionally problematic, on the ground that the bankruptcy power necessarily entails the power retroactively to impair contractual obligations and related liens.\textsuperscript{173}

\textsuperscript{169} See Gunn v. Barry, 82 U.S. (15 Wall.) 610 (1872); Jones v. Brandon, 48 Ga. 593 (1873); The Homestead Cases, 63 Va. (22 Gratt.) 266 (1872).


\textsuperscript{172} See In re Smith, 22 F. Cas. 413, 414 (C.C.N.D. Ga. 1876) (No. 12,996), aff'g 22 F. Cas. 390 (N.D. Ga. 1873) (No. 12,986); In re Jordan, 13 F. Cas. 1079, 1080 (W.D.N.C. 1873) (No. 7514); In re Kean, 14 F. Cas. 157, 157 (W.D. Va. 1873) (No. 7630).

\textsuperscript{173} In re Smith, 22 F. Cas. 413, 414 (C.C.N.D. Ga. 1876) (No. 12,996), aff'g 22 F. Cas. 399 (N.D. Ga. 1873) (No. 12,986); In re Jordan, 13 F. Cas. 1079, 1080 (W.D.N.C. 1873) (No. 7514); In re Kean, 14 F. Cas. 157, 157 (W.D. Va. 1873) (No. 7630); In re Volger, 28 F. Cas. 1248, 1250 (W.D.N.C. 1873) (No. 16,986); In re
Thus, the nineteenth and early twentieth century bankruptcy cases belie the assertion in Security Industrial Bank that retroactive bankruptcy legislation impairing secured creditors' rights poses substantial fifth amendment problems. Only the Radford case supports the view that the fifth amendment operates as an independent source of limitations on retroactive application of the bankruptcy power, and Radford itself marked a radical and unexplained shift in the analysis of the relationship between the bankruptcy clause and the fifth amendment.174 Given that Radford's specific application of fifth amendment retroactivity principles was essentially overruled by the subsequent Frazier-Lemke Act cases,175 one might suggest that Radford's analytic assumptions should also be regarded as little more than a sport.

2. The Security Industrial Bank Analysis. — Nevertheless, in light of Security Industrial Bank, it appears that the Supreme Court will continue to accept at least the general principle for which Radford stands — that the fifth amendment may impose some limitations on the retroactive application of bankruptcy legislation — although the Court's reasons for doing so are not entirely clear. It is not, however, particularly easy to derive from Security Industrial Bank any useful principles for delineating those limitations. The Court's analysis seems to comprise two steps. First, Justice Rehnquist noted that a creditor's security interest in personal property of the debtor is recognized as a property interest under the relevant state law,176 and observed that section 522(f)'s invalidation of

Wyllie, 30 F. Cas. 733, 737 (W.D. Va. 1872) (No. 18,112) (dictum). There appears to be only one case, In re Dillard, 7 F. Cas. 703 (C.C.E.D. Va. 1873) (No. 3912), that ruled that the 1873 Act would be invalid on fifth amendment principles if applied retroactively. The case therefore limited the Act to prospective application, id. at 706. Justice Rehnquist's opinion in Security Industrial Bank completely overlooks the cases dealing with the 1873 amendment, notwithstanding the fact that, to the extent that both the 1873 amendment and § 522(f) of the new Bankruptcy Code invalidated judicial liens on exempt property, the issues presented by the two provisions were identical.

174 One might seek to explain the Radford shift on the ground that the 19th century bankruptcy cases were decided before Pennsylvania Coal Co. v. Mahon, 260 U.S. 393 (1922), the first decision stating that a nonappropriative regulatory measure might violate the takings clause, see J. NOWAK, R. ROTUNDA & J. YOUNG, HANDBOOK ON CONSTITUTIONAL LAW 440-42 (1978). The problem with this explanation is that the Rock Island case, decided 13 years after Pennsylvania Coal, reaffirmed the analysis applied in the pre-Radford cases. See supra p. 1004. Moreover, Pennsylvania Coal was not even cited in Radford, and Justice Brandeis, the author of Radford, dissented in Pennsylvania Coal, see 260 U.S. at 416-22 (Brandeis, J., dissenting).

175 See supra pp. 980-81 & note 54.

176 103 S. Ct. at 411 n.6.
such a security interest amounts to a "complete destruction of the property right of the secured party." Accordingly, the Court regarded cases involving restrictions on only "some but not all of the 'bundle of rights' which comprise the 'property' in question" to be largely irrelevant. Second, Justice Rehnquist considered the government's contention that, because the security interests invalidated by section 522(f) were likely to be used principally as a bargaining lever against the debtor rather than as a source of repayment of the debt, retroactive application of section 522(f) did not violate the takings clause. The opinion states that, although this argument "cannot be dismissed out of hand," it is belied by the state law categorization of the security interests as property, a categorization on which takings analysis must rely. Both steps in this analysis are flawed.

(a) Complete Versus Partial Destructions of Property Rights. — The key to Justice Rehnquist's analysis in Security Industrial Bank seems to be the assertion that the case involved a complete destruction of a property interest. Yet an analysis based upon the distinction between complete and partial destructions of property interests quickly redounds to circularity, for the distinction depends entirely on the definition of the property interests involved. In Security Industrial Bank, Justice Rehnquist distinguished Penn Central Transportation Co. v. City of New York — which upheld the application of New York City's Landmarks Preservation Law to prevent construction of an office tower atop Grand Central Station — on the ground that the legislation in the earlier case only partly impaired the owner's rights in the parcel of real estate affected. Yet Penn Central could just as well be described as a case in which the value of the air rights above the existing parcel were completely or nearly completely destroyed. Similarly, a zoning law imposing setback requirements can be described either as a partial impairment of the owner's rights

177 Id. at 411.
178 Id. (referring to Penn Cent. Transp. Co. v. City of New York, 438 U.S. 104 (1978)).
179 Id. at 412.
180 Id.
in the entire parcel or as an essentially total destruction of the value of the portion on which construction is prohibited.

The attempt to use the distinction between complete and partial destructions as the key to the analysis of the constitutionality of retroactive legislation proves no more successful in explaining the result reached in *Security Industrial Bank* itself. Justice Rehnquist's characterization of section 522(f) as a measure that completely destroyed the secured creditor's property right depends entirely on an arbitrary definition of the scope of the property interest involved. In the first place, section 522(f) applies only in bankruptcy proceedings; hence the secured creditor's lien remains fully effective in other contexts. Moreover, section 522(f) invalidates security interests only in certain property specified by type and value, and thus would effect only a partial invalidation of the security interest of a creditor holding a lien on a more extensive set of collateral. Nothing in the Court's opinion, however, suggests that the constitutional issue was seen to be limited to creditors holding liens only on property covered by section 522(f).

The most serious flaw in Justice Rehnquist's attempt to apply the distinction between complete and partial destructions in *Security Industrial Bank* is that, even if all of the secured creditor's collateral were affected by section 522(f), the creditor would retain an unsecured claim against the debtor and therefore would have an interest, in common with other unsecured creditors, in all of the debtor's nonexempt property. As has been argued above, there is no sound basis for contending that the interest of unsecured creditors in the debtor's estate as a whole is any less of a property interest than is the interest of secured creditors in their specific collateral. Thus, if the secured creditor's "property" interest is properly viewed as his total claim against the debtor's assets, even complete invalidation of the creditor's lien does not effect a complete destruction of his property interest.

(b) Nature of Property Interests Destroyed. — The second step of the analysis in *Security Industrial Bank* is even less consistent with established takings clause jurisprudence than is the first step. The opinion seems to suggest that, because state law categorizes the security interests in question as property interests, it is irrelevant to the takings analysis that the only value of the security interest to the creditor may be in coercing the debtor into a reaffirmation of the debt by threat-
ening to deprive the debtor of his household furnishings.\textsuperscript{187} There is, however, nothing in takings clause jurisprudence suggesting that the mere state law categorization of an interest as property obviates the need to consider whether the property interest regulated or destroyed is one that imposes inordinate harms on others. To the contrary, it is well established that such an inquiry is often decisive in takings analysis.\textsuperscript{188}

Thus, taken literally, the analysis of \textit{Security Industrial Bank} is neither consistent with sound takings clause analysis nor particularly helpful in specifying the permissible limits of retroactive bankruptcy legislation. Accordingly, I now turn to the consideration of a more satisfactory analytic framework, with which the result, though not the language, of \textit{Security Industrial Bank} is entirely consistent.

\textbf{B. An Alternative Approach}

\textit{I. The Relationship Between the Takings Clause and the Due Process Clause.} — To begin with, it is worth noting that constitutional constraints on retroactive legislation need not be attributed to the takings clause. Rather, constitutional retroactivity principles are often traced to the due process clause. In \textit{Usery v. Turner Elkhorn Mining Co.},\textsuperscript{189} for example, the Supreme Court analyzed solely as a matter of due process a challenge to the retroactive aspect of a federal statute requiring mine owners to compensate former employees afflicted by black lung disease.\textsuperscript{190}

Indeed, until the 1920's, it would have been virtually impossible to base a viable challenge to retroactive application.

\begin{itemize}
\item \textsuperscript{187} See 103 S. Ct. at 412.
\item \textsuperscript{189} 428 U.S. 1 (1976).
\item \textsuperscript{190} See id. at 16-17. Commentators have generally noted that the due process retroactivity test turns on a flexible balancing test, which considers such factors as the strength of the public interest served by the challenged statute, the need for retroactive application in order to achieve the purposes of the statute, the extent of the impairment of preenactment rights, and the extent to which parties have reasonably and legitimately relied on the preenactment system of legal rules. \textit{See Hochman, The Supreme Court and the Constitutionality of Retroactive Legislation}, 73 HARV. L. REV. 692 (1960); \textit{Slawson, Constitutional and Legislative Considerations in Retroactive Lawmaking}, 48 CALIF. L. REV. 216 (1960).\end{itemize}
of a bankruptcy statute on the takings clause. At the time when the takings clause was regarded to be applicable only to governmental action that involved an actual appropriation or physical invasion of property, most forms of harm to preexisting private economic interests that resulted from otherwise valid exercises of governmental power would not have been seen to raise problems under the takings clause, although non-appropriative retroactive legislation might have been considered invalid under the due process clause. Since the time of Pennsylvania Coal Co. v. Mahon, however, it has been a part of our constitutional theory that any sort of governmental regulation, if it "goes too far," may amount to a taking for which compensation must be provided. Thus, given a sufficiently broad conception of property, virtually any challenge to retroactive legislation that adversely affects economic interests can now be phrased as a matter of regulatory takings law.

The choice between the takings clause locution and the due process formulation, however, probably reflects only factual differences concerning the challenged legislation rather than any significant difference in the appropriate analysis. The effect of regulatory legislation on private economic interests can be alleviated in two ways: by limiting the legislation to prospective effect or by paying compensation for the impairment of preexisting interests. In cases that involve statutes regulating the use of land — which by their very nature cannot be limited to truly prospective effect — the only ameliorative option is the payment of compensation, and hence the takings clause description seems apt. On the other hand, in cases involving legislation such as the statute in Turner Elkhorn Mining, which required mine owners to pay benefits to former employees afflicted by black lung disease, a requirement of compensation would render pointless the legislation imposing a burden on private economic interests. Thus, when the only practical ameliorative option is to limit a measure to prospective application, the question of the measure's constitutionality is more likely to be phrased as a due process retroactivity issue than as a takings issue. In a wide variety of cases, however,

192 See Hochman, supra note 190, at 694 & n.15.
193 260 U.S. 393 (1922).
194 Id. at 415.
195 See supra note 59.
either formulation will be available, and nothing will turn on the choice of analytic reference.\(^{196}\)

The _Radford_ case\(^{197}\) itself illustrates the irrelevance of the choice between the takings clause and the due process clause in the analysis of retroactive legislation. Although courts and commentators generally have viewed _Radford_ as a takings clause decision,\(^{198}\) the _Radford_ opinion belies the suggestion that the Supreme Court saw the case solely as a takings clause matter. Justice Brandeis' opinion does not actually cite any takings clause cases,\(^{199}\) and there are passages in the opinion suggesting that the determinative precedents were contracts clause cases\(^{200}\) and due process cases.\(^{201}\) Indeed, the only explicit reference to the takings clause in _Radford_ comes in the opinion's concluding sentences,\(^{202}\) which may well be more a matter of rhetorical flourish than constitutional analysis. After all, any opinion holding economic legislation unconstitutional under the due process clause can be made to sound a bit more statesmanlike by the suggestion that the legislature is free to pursue the objectives of the legislation provided it is willing to pay the piper.

2. **Core Expectations.** — Whether one prefers the takings clause locution or the due process formulation, the core of the analysis of the constitutionality of retroactive legislation should

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\(^{196}\) In particular, it must be kept in mind that the possibility that due process or takings clause principles might limit the permissibility of retroactive alterations of bankruptcy law does not depend upon, or lend any support to, the notion that secured creditors' "property" rights are different, as a constitutional matter, from unsecured creditors' "contractual" claims. In this Article's discussion of the constitutional principles applicable to the substance of prospective bankruptcy legislation, the argument that there is a difference of constitutional dimension between the rights of secured creditors and those of unsecured creditors has been considered and rejected. *See supra* pp. 988–95. That discussion is equally applicable in the present setting of the constitutionality of retroactive changes in bankruptcy law. Both secured and unsecured creditors have "property" rights that could conceivably be entitled to protection against retroactive application of legislation effecting extreme, adverse changes of their rights in bankruptcy, whether one wishes to locate the source of retroactivity principles in the due process clause or in the takings clause.


\(^{198}\) See sources cited *supra* note 25.

\(^{199}\) There is, for example, no mention of Pennsylvania Coal Co. v. Mahon, 260 U.S. 393 (1922). Counsel for the bank in _Radford_ also appears to have argued for the unconstitutionality of the Frazier-Lemke Act solely on the bases of the bankruptcy clause, *see supra* 295 U.S. at 558–60, and the due process clause, *see id.* at 561.


\(^{201}\) See *id.* at 601 (citing Ochoa v. Hernandez y Morales, 230 U.S. 139 (1913)).

\(^{202}\) *Id.* at 601–02, *quoted at supra* note 25.
be the concern with disruption of the settled expectations of private parties. For example, in one of the most important recent examinations of the theoretical foundations of the takings clause, Professor Michelman suggests that the clause can be viewed as a provision designed to ensure that parties can rely on their economic expectations to the extent necessary to make productive activity worthwhile. 203 Similarly, in one of the Supreme Court's recent takings clause decisions, *Penn Central Transportation Co. v. City of New York*, 204 the Court indicated that one of the major factors in determining whether a taking has occurred is "the extent to which the regulation has interfered with distinct investment-backed expectations." 205 Proper analysis of retroactivity problems therefore turns largely on two issues: the extent to which the challenged legislation disrupts expectations and the legitimacy of those expectations.

It is sometimes suggested that the question of the extent to which a given statute disrupts legitimate expectations raises a purely quantitative inquiry. For example, in the takings context, the diminution of value test, 206 which is traceable to Justice Holmes' suggestion in *Pennsylvania Coal Co. v. Mahon* that a regulatory measure may be held a taking "if [the] regulation goes too far," 207 is often understood to ask how much the value of the property in question has been diminished by the challenged regulation. It is, however, more useful to view the question of the extent of disruption of expectations as a qualitative inquiry. For example, in some land use regulation cases the focus is not so much on the extent of the loss imposed, but on whether there are any remaining profitable uses for the land as regulated. 208 This residuum or remaining-feasible-use approach 209 seems to rest on the notion that there are certain core expectations involved in the ownership of land and in other economic activity and that it is these core expectations that are entitled to constitutional protection against retroactive disruption. The qualitative view seems to have played a decisive role in the Supreme Court's decision in *Penn*

205 Id. at 124.
207 260 U.S. at 415.
Central. Noting that the ordinance permitted Penn Central to continue to use Grand Central Station as it had been used since its construction and that this remaining use preserved Penn Central's opportunity to earn a reasonable return on its investment, the Court stated that "the law does not interfere with what must be regarded as Penn Central's primary expectation concerning the use of the parcel." 210

The usefulness of core expectations analysis to retroactivity problems depends, of course, on the ability to specify the relevant core or primary expectations. An effort to identify the core expectations embodied in the general concept of property may well be futile and, in any event, is beyond the scope of this Article. By limiting the inquiry to the context of secured creditors' rights in bankruptcy, however, one can develop a satisfactory analysis of the retroactivity issue.

The essential function of security for debts is the allocation of risk. 211 A secured creditor bargains for the right to limit his exposure to the general business risks of his debtor's enterprise, and, in return, charges a lower rate of interest or makes loans that would not otherwise be available to the debtor. This allocation of risk is implemented in our legal system by giving the secured creditor a prior claim against specific assets of the debtor; as has been noted above, 212 however, this mechanism is perhaps best viewed as simply a convenient, but not logically essential, means of allocating to other creditors or investors a larger portion of the risk of a deterioration in the debtor's earning capacity. 213 It seems plausible, therefore, that this allocation of risk — the secured creditor's

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210 438 U.S. at 136.
212 See supra pp. 993-94.
213 In many contexts other than the matter of supposed constitutional protections of secured creditors' rights, the law has not been blind to the difference between the essential function of security devices and the means by which that function is accomplished. For example, the development of the equity of redemption in mortgage law, see 1 L. JONES, A TREATISE ON THE LAW OF MORTGAGES OF REAL PROPERTY §§ 7-16 (8th ed. 1928), is a striking instance of the ability of the courts to disregard the consequences of the property law forms by which security devices were implemented in an effort to achieve more just results consistent with the central functions of the arrangements.

Other illustrations are provided by the long-established doctrine that parol evidence may be used to show that a bill of sale in absolute form was intended as a security device, see U.C.C. § 9-203 comment 4 (1977), and by various aspects of article 9 of the Uniform Commercial Code, such as the insistence that title concepts are irrelevant in determining the rights of parties to security arrangements, id. § 9-202, and the inclusion within the coverage of article 9 of any arrangement, however described or implemented, that has the effect of a security arrangement, id. § 9-102.
right to priority over other creditors and investors — should be regarded for constitutional purposes as the core of the secured creditor's expectations.

Accordingly, retroactive application of a provision of bankruptcy law that impairs the risk allocation function of security arrangements might raise substantial constitutional questions. That was precisely the problem in Security Industrial Bank: by invalidating liens, section 522(f) frustrates the secured creditor's effort to acquire priority for his claim by obtaining a security interest in the debtor's property. It is this disruption of the secured creditor's core expectations, and not the notion of a supposed distinction between complete and partial destructions of property interests, that might have proved the starting point for a sound analysis in Security Industrial Bank.

3. Legitimacy of Expectations. — The second aspect of a proper analysis of retroactivity problems is the inquiry into the legitimacy of the expectations disrupted. For example, land use regulations that restrict the use of property so severely that they destroy nearly all of its value have often been upheld against takings clause attack on grounds analogous to the nuisance concept that no one is entitled to use his property in a way that harms others. Distinguishing, at a very general level, between legitimate and illegitimate expectations is, to be sure, no easy task. Nonetheless, the imprecision of analysis attributable to the need to weigh genuinely relevant factors is certainly preferable to the false precision that results from basing the analysis on arbitrary concepts of property rights. Moreover, by focusing on the specific area of bankruptcy legislation, one can identify a useful approach to the analysis of legitimacy of expectations. In the first place, nothing in either Security Industrial Bank or Radford purports to overrule the pre-Radford cases that so readily upheld retroactive bankruptcy legislation impairing the rights of both secured and unsecured creditors. Thus, the recognition that we have a longstanding tradition of upholding the retroactive application


215 For critical discussion of the noxious use and prevention-of-harms tests in takings law, see Michelman, supra note 181, at 1196-201, 1235-45; Sax, supra note 181, at 48-50.
of new or amended bankruptcy statutes suggests that a creditor who contends that retroactive application of a change in the bankruptcy law would disrupt his legitimate expectations in a manner that would violate the Constitution should bear a very heavy burden of persuasion.\(^{216}\) Moreover, the evolution of bankruptcy legislation has been marked by an increasing recognition of the appropriate role of government in limiting certain aspects of creditors' rights against the debtor. Accordingly, as the creditors' rights at issue approach areas that have been marked as proper spheres of restriction by bankruptcy legislation, the less compelling are the creditors' claims of legitimate reliance.

Consider the disruption of expectations effected by the statute involved in *Security Industrial Bank*. The central principle of straight bankruptcy is that, to enable the debtor to make a fresh start, the government may limit the extent to which a debtor's assets will be devoted to the satisfaction of his creditors' claims.\(^{217}\) Before the enactment of the 1978 Bankruptcy Code, bankruptcy law generally allowed otherwise valid liens to be enforced against exempt property.\(^{218}\) This consideration may suggest that there is nothing illegitimate about a secured creditor's expectation that his priority could be established even through a mechanism that might impair the debtor's exemptions. Nonetheless, the theory of section 522(f) is that a lender who takes a non-purchase-money security interest in property such as a consumer's household goods probably does not actually anticipate that his security interest will have any substantial economic value as a priority mechanism, but hopes instead to be able to use the threat of repossession to coerce the debtor into agreeing to favorable settlements or reaffirmation agreements.\(^{219}\) Assuming that Congress accurately perceived the mischief that section 522(f) was designed to avoid, retroactive application of that provision would disrupt only the lender's expectation of being able to frustrate the fresh start policy. Certainly the sphere of legitimate expectations does not extend to the hope of being able

\(^{216}\) Cf. *Chevron Oil Co. v. Huson*, 404 U.S. 97, 106 (1971) (whether judicial decision overruling precedent should be given retroactive effect depends in part on whether decision was foreshadowed); Michelman, *supra* note 181, at 1240-41 (discussing theory that compensation is not required if society forewarns investor of possibility of destruction of his investment).

\(^{217}\) See *supra* p. 1001.

\(^{218}\) See *Collier, supra* note 7, ¶ 522.27, at 522-66 n.1; *Collier on Bankruptcy* ¶ 6.12, at 863 (J. Moore 14th ed. 1978).

to manipulate normally sanctioned legal devices in order to frustrate established governmental policy. Therefore, even the result in Security Industrial Bank may have been wrong.\footnote{On the other hand, one might argue that § 522(f) may disrupt legitimate expectations and that other mechanisms were available to Congress to deal more precisely with only those instances in which security interests in exempt property were being used for illegitimate purposes. Thus, § 722 of the Bankruptcy Code, 11 U.S.C. § 722 (Supp. V 1981), would permit the debtor to redeem exempt property subject to a security interest by paying the creditor the fair market value of the property, and § 524(c)-(d), 11 U.S.C. § 524(c)-(d) (Supp. V 1981), severely restricts the creditor's ability to obtain reaffirmation agreements.}

\section*{C. Retroactive Application of Legislation Authorizing Interim Restraint of Secured Creditors' Rights}

The analysis developed above would readily dispose of the constitutional issues that would be posed if Congress chose to abandon the adequate protection model of the new Bankruptcy Code and adopted legislation, with retroactive application, authorizing the type of impairment of secured creditors' rights that was involved in \textit{Yale Express}.\footnote{In re \textit{Yale Express Sys.}, 384 F.2d 990 (2d Cir. 1967). An attempt to analyze the problem under the language of \textit{Security Industrial Bank} would seem to be wholly inconclusive since such legislation would not entirely invalidate the secured creditor's lien. An attempt to apply some quantitative version of the diminution test, \textit{see supra} p. 1024, would lead to a fruitless attempt to specify the point at which depreciation in the value of the secured creditor's collateral becomes constitutionally problematic. For reasons discussed in Part I, \textit{see supra} pp. 995–97, identifying the requirement of preservation of the value of collateral as the critical point in a quantitative analysis would be wholly arbitrary.} In the first place, an order of the sort involved in \textit{Yale Express} would not significantly disrupt the core expectation of a secured creditor — the expectation that his security interest will enable him to implement the allocation of risk for which he has bargained. No one in \textit{Yale Express} denied that the secured creditor was entitled to priority over other claimants. Rather, mechanisms were devised to provide a substantial degree of assurance that the contractual risk allocation that the security interest was designed to implement would be preserved even if the specific collateral were not. If the reorganization succeeded, the creditor's claim was to be treated in the plan as a secured claim to the extent of the value of the collateral at the inception of the proceedings.\footnote{\textit{See} 384 F.2d at 992.} Even if the reorganization effort failed and the debtor's assets were liquidated, it appears that the creditor was to be given a priority claim for the amount of depreciation of the collateral.\footnote{\textit{See id.}} To be sure, if the court's prediction of the
likelihood of a successful reorganization had been incorrect, the secured creditor's priority position might have been impaired. The takings clause, however, does not provide insurance against the possibility of harm to private economic interests that results from the inevitable fallibility of governmental decisionmakers.224

Retroactive application of bankruptcy legislation authorizing the type of impairment of secured creditors' rights that was involved in *Yale Express* would, of course, disrupt certain expectations of secured creditors — specifically, the expectation that the creditor will have the power to seize his collateral upon the debtor's default in order to protect the limitation of risk for which he has bargained. Yet if the property involved is essential to any effort to effect a reorganization, the secured creditor's expectation of being able to seize the property is tantamount to an expectation of being able to decide whether the debtor should be permitted to attempt a reorganization. The development of bankruptcy legislation has been marked by an increasing recognition of the desirability of preserving the going concern value of enterprises.225 A creditor's expectation of being given veto power over the continued expansion of the means through which this objective of the bankruptcy system is pursued would certainly not rank high on the scale of legitimate expectations.

Moreover, looking to analogies drawn from areas other than bankruptcy law, one can find ample support for denying constitutional protection to a secured creditor's expectation of being given unilateral authority to decide whether to sacrifice the prospect of salvaging going concern values in order to ensure absolute protection of his own interests. In a wide variety of contexts, the legal system has developed significant limitations on the extent to which contractual agreements may give one party the authority to make decisions affecting the interests of others solely on the basis of his own interests. For example, the development of the concepts of unconscionability and good faith performance in the law of contracts can be seen as a manifestation of the concern with contractual agreements that permit one party to disregard entirely the interests

224 See *Keokuk & Hamilton Bridge Co. v. United States*, 260 U.S. 125 (1922) (person who sustains damages caused by government agency's tortious activity cannot avoid sovereign immunity bar by contending that the destruction of his property constitutes a taking). Although the loss of use of real estate caused by repeated low-altitude flights of military aircraft may be a compensable taking, United States v. *Causby*, 328 U.S. 256 (1946), no one would suppose that the complete destruction of a house caused by the crash of a military aircraft would be a taking.

225 See *supra* pp. 1001–05.
of another party in making decisions concerning the contractual relationship. Much the same concern can be seen in developments in corporate law imposing fiduciary duties on majority stockholders that restrain their ability to take action prejudicial to the interests of minority stockholders. In short, the secured creditor's contractual right to foreclose on the collateral to protect his own interests at the expense of destroying the going concern values from which other creditors might be paid is precisely the sort of contractual arrangement that in many areas of the law has been considered particularly troublesome. Thus, there is little reason to believe that such a contractual right is constitutionally immune from retroactive abrogation.

Although the analysis in Security Industrial Bank reflects a somewhat wooden view of takings clause and property concepts, there is ample support in other cases for a more flexible analysis of the constitutionality of retroactive bankruptcy legislation. Such an analysis would focus on the extent of disruption of core expectations and the legitimacy of the expectations disrupted. Given that the outcome of Security Industrial Bank is in fact consistent with such an approach, the language of the opinion need not be viewed to preclude the application of an analysis of the sort suggested in this Article in future cases involving retroactive bankruptcy legislation.

IV. CONCLUSION

This Article has considered specific issues concerning the impairment of secured creditors' rights in reorganization proceedings in order to provide a framework for consideration of the more general issue of the relationship between the bankruptcy clause and the due process and takings clauses of the fifth amendment. The conclusion must be that Justice Brandeis' famous statement in the Radford case that "[t]he bankruptcy power . . . is subject to the Fifth Amendment," a


227 See, e.g., Singer v. Magnavox Co., 380 A.2d 969 (Del. 1977). Similarly, the law of liability insurance has in recent decades moved toward the position that, if an insurance contract gives the insurer the right to decide whether to settle or to litigate a claim against the insured, the insurer must take account of the interests of the insured in making that decision. See 14 G. COUCH, CYCLOPEDIA OF INSURANCE LAW §§ 51.1–18 (M. Rhodes rev. 2d ed. 1982).

228 295 U.S. at 589.
statement that at first blush seems to be such a truism, is in fact false. The only significant constitutional restraint on the substance of purely prospective bankruptcy legislation is the bankruptcy clause itself. Even in the context of retroactive application of bankruptcy legislation, the effort to deduce controlling principles from general principles about property rights — as suggested by the language of Security Industrial Bank — proves far less successful than an approach that draws more heavily on bankruptcy principles in considering whether legitimate expectations are disrupted.

One of the most intriguing observations to be drawn from a study of the early cases in which the constitutionality of bankruptcy legislation was challenged is the remarkable transformation that has occurred in the style and language of constitutional analysis. No longer does one find challenges to the constitutionality of bankruptcy legislation phrased as contentions that the measure in question is not "a law on the subject of bankruptcy." Rather, since the time of Radford, the inquiry has shifted to the question whether the act at issue takes property rights in violation of general principles sought to be deduced from a theory of the takings clause.

Yet the attempt to use general fifth amendment concepts as a source for deriving specific principles limiting the bankruptcy power has led only to arbitrary and unsatisfactory results. Thus, there may have been far more wisdom than is now generally recognized in the concentration of nineteenth century lawyers and judges on specifying the scope of the powers implicit in the constitutional grant to Congress of authority over the subject of bankruptcies. Indeed, there may well be lessons here that extend beyond the subject of bankruptcy, for the shift of emphasis from the bankruptcy clause to the fifth amendment may be but one manifestation of the abandonment of any serious effort to regard government (federal or state) as having only specific granted powers whose scope is limited by the terms of the explicit or implicit grant, rather than as possessing plenary powers over all human endeavors, restricted only by specific limiting principles. That larger issue, however, is a matter for another day.