

# OF PROGRESSIVE PROPERTY AND PUBLIC DEBT

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## INTRODUCTION

People should pay their debts.<sup>1</sup> The Bible tells us to pay a man what he is owed.<sup>2</sup> Ralph Waldo Emerson advised that we should “pay every debt as if God wrote the bill[.]”<sup>3</sup> Even in popular culture we are told that “[a] Lannister always pa[ys] his debts.”<sup>4</sup>

As a society, we inherently feel that people have a moral duty to fulfill their financial obligations—to pay their debts.<sup>5</sup> Indeed, the ability to enforce obligations between private parties is deeply tied to the idea of the rule of law—that society orders itself in a way, through the instrument of law, that allows parties to enter into agreements with one another and to have those agreements enforced.<sup>6</sup> At the heart of the rule of law is property

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1. HOWARD DAYTON, *YOUR MONEY COUNTS* 36–37 (1996).

2. *Romans* 13:7 (New American) (“Pay to all their dues, taxes to whom taxes are due, toll to whom toll is due, respect to whom respect is due, honor to whom honor is due.”).

3. Ralph Waldo Emerson, *Suum Cuique*, in *HOYT’S NEW CYCLOPEDIA OF PRACTICAL QUOTATIONS* 181, 181 (Kate Louise Roberts ed., 1940).

4. See GEORGE R.R. MARTIN, *A GAME OF THRONES* 330 (1996).

5. See, e.g., DAYTON, *supra* note 1, at 51 (“Godly people should pay their debts and bills as promptly as they can. We have a policy of trying to pay each bill the same day we receive it to demonstrate to others that knowing Jesus Christ has made us financially responsible.”).

6. Robert A. Stein, *The Rule of Law*, in *THE RULE OF LAW IN THE 21ST CENTURY* 11, 11–14 (Robert A. Stein & Richard J. Goldstone eds., 2015); see generally Nadia E. Nedzel, *The Rule of Law: Its History and Meaning in Common Law, Civil Law, and Latin American Judicial Systems*, 10 *RICH. J.*

law.<sup>7</sup> The right of the creditor to demand payment and the obligation of the debtor to comply accordingly are rooted in a sense of fidelity to property rights.<sup>8</sup> The creditor has a right in the debt—the right to claim payment—and the debtor has an obligation to respect that property right—a right that imposes a burden on him to make tender.<sup>9</sup> Property rights fundamentally shape society, so it is no surprise that the “debt-as-property” concept underpins our larger moral feelings about the obligation to meet one’s debts.

But, it is not *always* true that we think debts should be paid. There may be situations where a less individualistic view of property or debt is necessary. For instance, our fidelity to the concept might change depending on whether we find the debt to be odious because of how it was acquired or because respecting the rights of the creditor will negatively affect society at large or otherwise impede broader policy goals that we find important.<sup>10</sup> To make this concept less abstract, consider the following example. The deadly disease of malaria at one time plagued the people of Madagascar but has since been quelled by the introduction of a vaccine.<sup>11</sup> Over the years, however, generations of people on the island—having not seen an outbreak of malaria in many years—ceased to be immune to the disease.<sup>12</sup>

Fast forward to the 1970s. As a result of an international economic downturn, the country was hit with hard times and had to borrow heavily from the financial markets in order to continue its development programs.<sup>13</sup> The International Monetary Fund, one of the island’s most powerful creditors, required a severe austerity program as part of its financing.<sup>14</sup> This included completely cutting the government program that conducted periodic testing of

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GLOBAL L. & BUS. 57 (2010) (discussing how cultural differences influence the development of the common law and civil legal systems).

7. JEREMY BENTHAM, *Principles of the Civil Code*, in 1 THE WORKS OF JEREMY BENTHAM 297, 309 (John Bowring ed., 1843) (“Property and law are born and must die together.”).

8. See Elizabeth Warren, *A Principled Approach to Consumer Bankruptcy*, 71 AM. BANKR. L.J. 483, 483 (1997).

9. See *id.*

10. For a discussion of the concept of odious debt, see, for example, ODETTE LIENAU, *RETHINKING SOVEREIGN DEBT* 1 (2014); Lee C. Buchheit et al., *The Dilemma of Odious Debts*, 56 DUKE L.J. 1201, 1205–07 (2007); Anna Gelpern, *Odious, Not Debt*, L. & CONTEMP. PROBS., 2007, at 81, 81–83; Seema Jayachandran & Michael Kremer, *Odious Debt*, 96 AM. ECON. REV. 82, 82–83, 91 (2006).

11. See DAVID GRAEBER, *DEBT: THE FIRST 5,000 YEARS* 4 (2011).

12. See *id.*

13. Tom Masland, *Malaria Deaths on Rise in Africa*, CHI. TRIB. (June 4, 1989), [http://articles.chicagotribune.com/1989-06-04/news/8902060639\\_1\\_malaria-madagascar-africa](http://articles.chicagotribune.com/1989-06-04/news/8902060639_1_malaria-madagascar-africa).

14. See GRAEBER, *supra* note 11, at 4.

mosquitos and cyclical spraying.<sup>15</sup> Then, in the late 1980s, the island was hit with a lethal outbreak of malaria.<sup>16</sup> At the behest of its creditors demanding cuts to spending, the island closed five thousand of its eight thousand rural health centers and was only able to meet one-fourth of the demand for malaria-treating medication.<sup>17</sup> Over ten thousand people died—many of them children in their parents' arms—all so that debts could be paid.<sup>18</sup> One commentator notes that even though the island owed the debt, no one could possibly justify the deaths of thousands of people just “to ensure that Citibank wouldn't have to cut its losses on one irresponsible loan that wasn't particularly important to its balance sheet anyway.”<sup>19</sup> Indeed, anyone would find such a result highly offensive. People find this offensive because although society values property rights and the moral duty to fulfill one's obligations, society values human life more.<sup>20</sup> Because of this allocation of values, we sometimes find reasons to give debtors a fresh start or otherwise disfavor the rights of creditors—indeed that is what bankruptcy theory is all about.<sup>21</sup>

The perceived tension between property rights and human dignity is on high display in the context of a sovereign debt crisis.<sup>22</sup> Indeed, much has been written about the tremendous stakes at play

15. *See id.*

16. JAMES L.A. WEBB, JR., THE LONG STRUGGLE AGAINST MALARIA IN TROPICAL AFRICA 134–35 (2014).

17. Masland, *supra* note 13.

18. GRAEBER, *supra* note 11, at 4.

19. *See id.*

20. Warren, *supra* note 8, at 491–93.

21. *See id.* at 483 (describing how the two competing goals of bankruptcy, a “fresh start” for debtors and equality of distribution for debtors, are more than rhetorical for the National Bankruptcy Review Commission). *See generally* Local Loan Co. v. Hunt, 292 U.S. 234 (1934) (noting that the purpose of the Bankruptcy Act and filing for relief is not to bury debtors under mountains of debt); Nicholas L. Georgakopoulos, *Bankruptcy Law for Productivity*, 37 WAKE FOREST L. REV. 51 (2002) (discussing the productivity incentives that bankruptcy creates); Charles G. Hallinan, *The “Fresh Start” Policy in Consumer Bankruptcy: A Historical Inventory and an Interpretative Theory*, 21 U. RICH. L. REV. 49 (1986) (noting that, as a practical matter, the great majority of consumer bankruptcy proceedings produce little in payments to creditors); Margaret Howard, *A Theory of Discharge in Consumer Bankruptcy*, 48 OHIO ST. L.J. 1047 (1987) (considering the appropriate scope of the debt discharge system); Thomas H. Jackson, *The Fresh-Start Policy in Bankruptcy Law*, 98 HARV. L. REV. 1393 (1985) (discussing the wisdom of the discharge doctrine in modern bankruptcy law); Charles J. Tabb, *The Scope of the Fresh Start in Bankruptcy: Collateral Conversions and the Dischargeability Debate*, 59 GEO. WASH. L. REV. 56 (1990) (examining the economic benefits given to the debtor through the modern bankruptcy system).

22. SABINE MICHALOWSKI, UNCONSTITUTIONAL REGIMES AND THE VALIDITY OF SOVEREIGN DEBT 1 (2007); Matthias Goldmann, *Human Rights and Sovereign Debt Workouts*, in MAKING SOVEREIGN FINANCING AND HUMAN RIGHTS WORK 80, 83–86 (Juan Pablo Bohoslavsky & Jernej Letnar Cernic eds., 2014).

where the debt belongs to a country—rather than an individual—and how austerity can cause a heavy human toll to be exacted in order for debts to be repaid.<sup>23</sup> But is it true that property rights and human dignity concerns are strictly adversarial in a public debt crisis? In other words, is it that simple to say that creditors hold the high ground when it comes to the property rights argument and that the people and government of the distressed jurisdiction hold a similarly singular position in the argument for human dignity? If that is true, then bankruptcy is really all about forcing those holding property rights (i.e., creditors) to accept restrictions or diminishments of those rights in favor of the nonproperty interests of debtors.

In this Article, I reject such a juxtaposition of interests. Not only do creditors and debtors have property rights and human dignity claims in these insolvency battles but, in fact, property rights and human dignity concerns are not altogether different. They are intimately intertwined. The shaping, defining, and allocating of property rights are, by the very definition of property law, functions of how society values human dignity. Human values shape property rights, and property rights, far from being monolithic, are dynamic and embrace a host of societal concerns—including those involving the payment of debts.

To explain the reconciliation of property rights and human dignity concerns in the context of distressed public debt—as well as to show how a reformation of bankruptcy law's view of property is needed—this Article focuses on the current crisis in the Commonwealth of Puerto Rico.<sup>24</sup> As of summer 2016, Puerto Rico—

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23. See, e.g., MARK BLYTH, *AUSTERITY* 21 (2013); THOMAS BYRNE EDSALL, *THE AGE OF AUSTERITY* 13 (2012); FLORIAN SCHUI, *AUSTERITY: THE GREAT FAILURE* 1–3, 5 (2014); Daniel D. Bradlow, *Debt, Development, and Human Rights: Lessons from South Africa*, 12 MICH. J. INT'L L. 647, 647–48 (1991); Chrystin Ondersma, *A Human Rights Framework for Debt Relief*, 36 U. PA. J. INT'L L. 269, 272 (2014); Steven A. Ramirez, *Taking Economic Human Rights Seriously After the Debt Crisis*, 42 LOY. U. CHI. L.J. 713, 713–15 (2011); see also U.N. Conference on Trade & Dev., *Principles on Promoting Responsible Sovereign Lending and Borrowing* (Jan. 10, 2012), [http://unctad.org/en/PublicationsLibrary/gdsddf2012misc1\\_en.pdf](http://unctad.org/en/PublicationsLibrary/gdsddf2012misc1_en.pdf); Anna Gelpern, *Bankruptcy, Backwards: The Problem of Quasi-Sovereign Debt*, 121 YALE L.J. 888, 891 (2012).

24. See *infra* Part I. In this Article I do not address the need for a property theory reformation of nonpublic bankruptcy (such as consumer or business bankruptcy). The case for a rejection of the current property law rules in the context of business bankruptcy is made quite compellingly by Professor Charles Tabb. See Charles J. Tabb, *The Bankruptcy Clause, The Fifth Amendment, and the Limited Rights of Secured Creditors in Bankruptcy*, 2015 U. ILL. L. REV. 765, 766 (2015). Rather, I focus on public bankruptcy because of the tremendous and widespread harm that public insolvency can cause in society, and also because of the extreme difficulty in neatly classifying creditors into property and nonproperty categories when it comes to public insolvency (a task that is

an island and territory of the United States inhabited by 3.5 million American citizens—stands to default on its public debt to the tune of more than \$70 billion.<sup>25</sup> In the island's current economic state, it is almost certain that financial ruin lies on the horizon.<sup>26</sup> The situation has become so desperate that the Commonwealth has been forced to borrow even more money to meet its current obligations, as well as make massive cuts in almost every sector.<sup>27</sup> Austerity reigns, and bondholders have demanded more cuts as the country teeters on economic collapse.<sup>28</sup>

Congress and the President recently came to the aid of the island.<sup>29</sup> The Puerto Rico Oversight, Management, and Economic Stability Act ("PROMESA") creates a bankruptcy-like mechanism for Puerto Rico to restructure and manage its debts.<sup>30</sup> The bill was signed into law by President Obama on June 30, 2016—right on the eve of the island making an additional default of \$2 billion.<sup>31</sup> Nevertheless, the actual mechanics of how the law will work are anything but certain. In the face of this legislation, an aggressive dark money campaign was launched to kill the bill.<sup>32</sup> The groups backing this campaign claim, among other things, that PROMESA, and a subsequent debt modification, would violate their constitutionally protected property rights and be an outright affront to the rule of law.<sup>33</sup>

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more easily accomplished in nonpublic bankruptcies). See *infra* Part II and accompanying discussion.

25. See *infra* Part I.

26. See *infra* Part I.

27. See *infra* Subpart I.A.

28. See *infra* Subpart I.A.

29. Heather Long, *President Obama Signs Puerto Rico Rescue Bill*, CNN MONEY (June 30, 2016, 5:00 PM), <http://money.cnn.com/2016/06/29/investing/puerto-rico-debt-promesa/>.

30. See *infra* Subpart I.A and accompanying discussion.

31. Mary Clare Jalonick, *Obama Quickly Signs Puerto Rico Financial Rescue Bill*, ABC 33/40 (June 30, 2016), <http://beta.abc3340.com/news/nation-world/obama-quickly-signs-puerto-rico-financial-rescue-bill>; Long, *supra* note 29.

32. Michelle Ye Hee Lee, *A Dark Money Group's Misleading Claim That the Puerto Rico Debt Plan Is a 'Bailout.'* WASH. POST (May 10, 2016), <https://www.washingtonpost.com/news/fact-checker/wp/2016/05/10/a-dark-money-groups-misleading-claim-that-the-puerto-rico-debt-plan-is-a-bailout/>; Ctr. for Individual Freedom, *CFIF TV Next*, YOUTUBE (May 17, 2016), <https://www.youtube.com/watch?v=VNDVroDb0GY>; Ctr. for Individual Freedom, *Fast One*, YOUTUBE (Apr. 12, 2016), <https://www.youtube.com/watch?v=TBA-msVRXgw>.

33. See Marc Joffe, *With Puerto Rico, Get Over Your 'Principled Opposition,'* REAL CLEAR MARKETS (June 2, 2016), [http://www.realclearmarkets.com/articles/2016/06/02/with\\_puerto\\_rico\\_get\\_over\\_your\\_principled\\_opposition\\_102198.html](http://www.realclearmarkets.com/articles/2016/06/02/with_puerto_rico_get_over_your_principled_opposition_102198.html); *PROMESA "Super Chapter 9" Is Still A Bailout on the Backs of Bondholders Across America*, THE STREET (Apr. 15, 2016, 9:35 AM), <https://www.thestreet.com/story/13532363/1/promesa-super-chapter-9-is-still-a-bailout-on-the-backs-of-bondholders-across-america.html>; Benjamin Zycher,

In the face of these claims, the island nears a humanitarian crisis.<sup>34</sup> Rural areas are populated by ghost towns, with the island's total population shrinking 10% over the past decade.<sup>35</sup> More than 150 schools have been shut down in the past few years, and emergency rooms in hospitals across the Commonwealth report patients waiting in hallways for several days to a week before getting a room or receiving services.<sup>36</sup> Over 50% of the citizens rely on government-assisted healthcare, despite the fact that healthcare services on the island are reimbursed at disproportionately lower rates than those on the mainland.<sup>37</sup> The unemployment rate is over 12%,<sup>38</sup> and 40% of the island lives in poverty (with 56% of that being children).<sup>39</sup>

Like in so many other public debt debates, the island's financial crisis has been framed in terms of a two-sided tension—one between property entitlements (those of the bondholders) on the one hand and human dignity concerns (those of the people of the Commonwealth) on the other.<sup>40</sup> Bondholders argue that Congress is trying to bail out<sup>41</sup> Puerto Rico on the backs of everyday American seniors and savers, forcing them to take heavy losses and killing their investments.<sup>42</sup> The Puerto Rican government, on the other hand, argues that it is “out of cash” and that there is a “humanitarian crisis under the flag of the United States.”<sup>43</sup> The option, so the Puerto Rican governor states, is between paying creditors or continuing to provide critical services to the island.<sup>44</sup>

Opinion, *Puerto Rico Needs Compromise, Not a Cram-Down*, HILL (Apr. 6, 2016, 1:30 PM), <http://thehill.com/blogs/pundits-blog/finance/275358-compromise-not-a-cram-down-needed-for-puerto-rico>.

34. See *infra* Subpart II.B.

35. See *infra* Subpart II.B.

36. See *infra* Subpart II.B.

37. See *infra* Subpart II.B.

38. Douglas A. McIntyre, *Puerto Rico Unemployment at 12.6%, Poverty at 41%*, 24/7 WALL ST. (June 30, 2015, 6:23 AM), <http://247wallst.com/economy/2015/06/30/puerto-rico-unemployment-at-12-6-poverty-at-41/>.

39. See *infra* Subpart II.B.

40. Vann R. Newkirk II, *Will Puerto Rico's Debt Crisis Spark a Humanitarian Disaster?*, ATLANTIC (May 13, 2016), <http://www.theatlantic.com/politics/archive/2016/05/puerto-rico-treasury-visit/482562/>.

41. Anthony J. Casey & Eric A. Posner, *A Framework for Bailout Regulation*, 91 NOTRE DAME L. REV. 479, 479–80 (2015) (discussing the 2008 financial crisis bailouts and earlier bailouts in order to determine what policy considerations best justify them and how they can be best designed).

42. Ctr. for Individual Freedom, *CFIF "Crushed"*, YOUTUBE (Apr. 21, 2016), <https://www.youtube.com/watch?v=bv800uteRi8>.

43. CNN, *Puerto Rico Governor: 'We Are Out of Cash'*, YOUTUBE (Dec. 10, 2015), [https://www.youtube.com/watch?v=WYJ\\_Lm60yDI](https://www.youtube.com/watch?v=WYJ_Lm60yDI).

44. Michael A. Fletcher, *Puerto Rico's Financial Crisis Just Got More Serious*, WASH. POST WONKBLOG (Dec. 1, 2015), <https://www.washingtonpost.com/news/wonk/wp/2015/12/01/puerto-ricos-fiscal-crisis-just-got-more-serious/>.

This Article rejects such a framing of public debt crises as being unhelpful and too normatively constraining and, in doing so, reconstructs the debate as one that does not require “good guy”/“bad guy” labeling—but rather shows that each side has legitimate, compelling, and multifaceted claims. The bondholders and the Puerto Ricans each have varying degrees of property rights and human claims in this crisis.

But it is not enough to merely reframe the issues of property rights and human rights as being interlocking. The treatment of property rights in the bankruptcy process cannot be changed merely by a reframing of competing sides. Rather, it is necessary to fundamentally change how the law reconciles property claims and human dignity concerns in the resolution of public debt disputes. I do this by looking at the way bankruptcy law and property law interact in the context of modifying and restructuring debt through the lens of the Puerto Rican insolvency. In analyzing the distinction that the Supreme Court has made between certain classes of debt in interpreting the Takings Clause of the U.S. Constitution,<sup>45</sup> I argue that, from a normative perspective, current law has failed to adequately reflect the way that property rights are measured, informed, and shaped by concerns for human dignity.<sup>46</sup>

In joining others who have found fault with this unhelpful bifurcation of property rights in bankruptcy law,<sup>47</sup> I offer a new perspective when it comes to dealing with debt recomposition proceedings. I advocate that courts reform their view of property rights in bankruptcy and use the ideas found in the progressive property movement as the tool to do so. This body of scholarship

45. Doctrinally, the U.S. Supreme Court's decision in *Louisville Joint Stock Land Bank v. Radford*, 295 U.S. 555 (1935), creates a division between contract rights that are property and contract rights that are nonproperty, *id.* at 560, 568, 589, but as explored in Part II, there are strong reasons to think this should not be the case.

46. In this Article I do not address how human dignity and private entitlements are or should be resolved under the Contracts Clause of the U.S. Constitution. While such a discussion is certainly needed in the literature, after the Supreme Court's decision in *Puerto Rico v. Franklin California Tax-Free Trust*, 136 S. Ct. 1938, 1942, 1945 (2016), it is clear that states cannot create their own bankruptcy procedures without violating federal preemption principles. Because the Contracts Clause only applies to the states (and not the federal government), it is not a constraint on the Bankruptcy Clause or municipalities who are able to seek cover under federal bankruptcy proceedings. See *U.S. Tr. Co. of N.Y. v. New Jersey*, 431 U.S. 1, 14–16 (1977).

47. See James Steven Rogers, *The Impairment of Secured Creditors' Rights in Reorganization: A Study of the Relationship Between the Fifth Amendment and the Bankruptcy Clause*, 96 HARV. L. REV. 973, 974–75 (1983); Tabb, *supra* note 24, at 808–09. As discussed in-depth in Subpart II.A, only debt that is secured by collateral is given Takings Clause protection within the context of bankruptcy. This is the case even though outside of bankruptcy all types of debt (secured or not) are considered constitutionally protected property.

stands for the notion that property rights are first and foremost concerned with human flourishing and that property, rather than being strictly individual in nature, has a social dimension that requires flexibility in interpretation so as to achieve just results and alignment with broadly shared human values.<sup>48</sup> By adopting such a progressive view and breaking down existing artificial barriers, the law will come not only to better define property rights, but also will have the practical effect of better accommodating the policy goals that lie at the heart of public debt recomposition in the United States.<sup>49</sup>

Seeking to achieve these ends, this Article proceeds as follows: Part I rejects the prevailing but false dichotomy between property rights and human dignity concerns. In order to contextualize this point and further discussion in this Article, Part I also gives an overview of the Puerto Rican debt crisis, its causes, and recent government responses, and then reconstructs the framing of the crisis by analyzing the dignity and property claims of both the Puerto Ricans and those holding Commonwealth debt. Having established the interlocking claims of these parties, Part II tests their resolution by analyzing the application of the Bankruptcy Clause<sup>50</sup> and the Takings Clause and argues that the Supreme Court's view of property rights in bankruptcy—specifically those of secured creditors—has become too constrained and fails to appreciate the ways in which human values inform and shape property rights, particularly related to the extreme human toll that a public debt crisis entails. Rather than approaching a creditor's rights under the rigid doctrines and inflexible rules that currently prevail, Part III—using the case of Puerto Rico and relying on scholarship arising from the progressive property movement—concludes by arguing that intrinsic human concerns should play a significant role in shaping the scope and allocation of property rights in public debt recomposition. Additionally, courts should be given a freer hand in dealing with such obligations. In adopting a broader, more progressive view of property rights when it comes to public debt, courts and Congress will be empowered to better help and protect the rights of all parties in times of serious financial distress.

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48. See *infra* Part II and III.

49. See *infra* Part III.

50. The text of PROMESA purports that the legislation is enacted under the Territories Clause of the U.S. Constitution. S. 2328, 114th Cong. (2016) (enacted). However, as I argue in Subpart III.A, I believe the more likely provision powering the PROMESA process is the Bankruptcy Clause. See *infra* Subpart III.A.

## I. THE FALSE DICHOTOMY OF PROPERTY RIGHTS AND HUMAN DIGNITY: A VIEW FROM PUERTO RICO

Like in so many public debt crises, opposing parties in the Puerto Rican saga have tried to reduce the situation to a simple case of one side versus the other—the bondholders versus the islanders.<sup>51</sup> Or, to put the argument in context, property rights versus human dignity.<sup>52</sup> The bondholders assert their rights in the debt and the need to uphold the rule of law and settled agreements, while the island's government and accompanying advocates raise the deteriorating state of life on the island and the dire straits of the Puerto Rican people.<sup>53</sup> This way of framing sovereign debt battles is not only counterproductive, but it is also overly simplistic.<sup>54</sup> It fails to appreciate the interlocking nature of human dignity and property rights, particularly the way in which an optimal theory of property calls for the embracing of more than just the rights of the individual.<sup>55</sup> Rather, human values and issues of human dignity play a significant role in the property question—concepts that play out writ large in the story of the Puerto Rican debt crisis.<sup>56</sup>

But in order to use the Puerto Rican debt crisis as a lens through which we can consider property rights and human dignity in public debt recomposition, it is necessary to know something about Puerto Rico and how its crisis came about. The following Subpart provides such an overview.

### A. Overview of the Puerto Rican Debt Crisis

Puerto Rico has been under the control of the United States since the late 1890s when it was invaded during the Spanish-American War.<sup>57</sup> However, the island was only slowly granted self-

51. See *infra* Subpart I.B.

52. See *infra* Subpart I.B.

53. See *infra* Subpart I.B.

54. See *infra* Subpart I.B.

55. See *infra* Subpart I.B.

56. See *infra* Subpart I.B.

57. MARC D. JOFFE & JESSE MARTINEZ, MERCATUS CTR., GEORGE MASON UNIV., ORIGINS OF THE PUERTO RICO FISCAL CRISIS 4 (Apr. 2016) (citing KAL WAGENHEIM & OLGA JIMENEZ DE WAGENHEIM, THE PUERTO RICANS 222–25 (2013)), <http://mercatus.org/sites/default/files/Joffe-Puerto-Rico-Fiscal-Crisis-v1.pdf>. The island was first ruled by Spain from the early 1500s through the late 1800s, but it was not until 1897 that Madrid granted Puerto Rico some level of autonomy in the conduct of its affairs. *Id.* at 3–4. A year later, during the Spanish-American War, the United States invaded the island, ejected the Spanish authorities, and imposed martial law. *Id.* at 4. Commentators note that although the United States held a number of territories (Arizona, New Mexico, and Oklahoma) at the time of its acquisition of Puerto Rico, Congress decided to treat Puerto Rico differently. *Id.* For instance, each of the other territories was allowed to elect the entirety of its legislatures. *Id.* This favorable treatment was even accorded to Hawaii—a landmass similarly situated to Puerto Rico. *Id.* at 4–5. Moreover, Congress

rule, with much of its day-to-day affairs being dictated by the federal government. Indeed, Congress waited quite some time before declaring that residents of Puerto Rico enjoyed the status of American citizens.<sup>58</sup>

Finally, in 1917 Congress passed the Jones-Shafroth Act, which granted citizenship to the islanders and gave them the ability to elect both houses of their legislature.<sup>59</sup> But among the many things this piece of legislation accomplished, one stands out as being particularly important. The Act exempted interest payments from any bonds issued by the island's government from taxation at the federal, state, and local levels.<sup>60</sup> This, of course, made the island's debt tremendously attractive—far more so than most American municipal debt.<sup>61</sup> This will later play a significant role in the island's current debt predicament.<sup>62</sup>

The Jones-Shafroth Act had a number of other negative consequences as well. Because all Puerto Ricans were now U.S. citizens, they could freely leave the island and move to the mainland.<sup>63</sup> In the 1920s, over forty thousand people left the island, with many more making the move after the conclusion of World War II.<sup>64</sup> This outmigration had, and continues to have, dire consequences for the island's economic health and future prosperity.<sup>65</sup>

granted the people of Hawaii U.S. citizenship while passing over the Puerto Ricans for the same treatment. *Id.* at 5.

58. *Id.* Much of the reason for this disparate handling is attributed to the fact that the American political elite mistrusted the ruling class of the island, which was mostly Spanish-speaking. *Id.* This sentiment is summed up well in a letter to the *New York Times* that was published during this period stating, "The people are a light-hearted, simple-minded, harmless, indolent, docile people, and while they gamble and are fond of wine, women, music, and dancing, they are honest and sober. . . . As Ignorant and simple as they are, they hope a chance of government will improve their miserable condition." *Id.* (quoting S.S. Harvey, Letter to the Editor, *Americanizing Puerto Rico*, N.Y. TIMES (Feb. 22, 1899), <http://query.nytimes.com/mem/archive-free/pdf?res=9D0CE2D6163DE433A25751C2A9649C94689ED7CF>).

59. *Id.*; see also Jones-Shafroth Act, Pub. L. No. 64-368, 39 Stat. 951 (1917), <http://www.legisworks.org/congress/64/publaw-368.pdf>.

60. JOFFE & MARTINEZ, *supra* note 57, at 5–6.

61. Tom Anderson, *Is your Bond Fund Invested in Puerto Rico?*, CNBC (June 30, 2015, 2:25 PM), <http://www.cnbc.com/2015/06/30/is-your-bond-fund-invested-in-puerto-rico.html> ("Some of the top-performing municipal bond funds over the past five years have held huge stakes in Puerto Rican debt. . . . U.S. bond funds have an \$11.3 billion total exposure to Puerto Rican debt as of June 29, according to mutual fund firm research Morningstar.").

62. See Scott Greenberg & Gavin Ekins, *Tax Policy Helped Create Puerto Rico's Fiscal Crisis*, TAX FOUND., TAX POL'Y BLOG (June 30, 2015), <http://taxfoundation.org/blog/tax-policy-helped-create-puerto-rico-s-fiscal-crisis>.

63. JOFFE & MARTINEZ, *supra* note 57, at 6.

64. *Id.*

65. See *id.*; see also Jens Manuel Krogstad et al., *Puerto Rico's Losses Are Not Just Economic, but in People, Too*, PEW RES. CTR., FACTTANK (July 1, 2015),

Another blow to the island came in 1920 when Congress passed the infamous Merchant Marine Act (“Jones Act”).<sup>66</sup> This law prevents foreign-flagged vessels from transporting goods between any U.S. territory (like Puerto Rico) and the mainland.<sup>67</sup> The result has been a tremendous increase in shipping costs and higher prices for products sent to the mainland U.S.<sup>68</sup> Despite these difficulties, Puerto Rico enjoyed a long period of economic prosperity due to the presence of a number of large American businesses with facilities on the island—mostly in the way of agricultural corporations like sugar plantations.<sup>69</sup>

Like much of the United States at the time, Puerto Rico was hit hard by the Great Depression and required a great deal of government spending to get back on track.<sup>70</sup> Under the island’s governor, Rexford Tugwell who was appointed by FDR, the federal government implemented a number of programs, including the creation of the Water Resources Authority (“PREPA”), the Aqueduct and Sewer Authority (“PRASA”), the Land Authority, the Government Development Bank (“GDB”)—a major player in the current crisis—and the Highway and Transportation Authority (“PRHTA”).<sup>71</sup> Each of these public corporations immediately began issuing debt in order to fund critical infrastructure needs.<sup>72</sup> PREPA immediately incurred \$20 million in debt to purchase all of the island’s major electrical utilities and related supply apparatus.<sup>73</sup> The other public corporations followed suit and began borrowing heavily.<sup>74</sup>

When Congress eventually turned full control of the island over to officials elected by the people of Puerto Rico, aggressive borrowing at the central and municipal level commenced.<sup>75</sup> To get an idea of the pace of this borrowing, consider that in 1913 the total amount of central and municipal government debt on the island was \$5.8 million, and by 1931 that number ballooned to just under \$50 million, then dropped to just under \$25 million near the mid-1900s.<sup>76</sup> Nevertheless, the debt of public corporations remained

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<http://www.pewresearch.org/fact-tank/2015/07/01/puerto-ricos-losses-are-not-just-economic-but-in-people-too/>.

66. JOFFE & MARTINEZ, *supra* note 57, at 6.

67. See 46 U.S.C. § 30104 (2012).

68. JOFFE & MARTINEZ, *supra* note 57, at 6.

69. *Id.* (citing JAMES L. DIETZ, *ECONOMIC HISTORY OF PUERTO RICO* 111 (1986)).

70. *Id.* at 6–7.

71. *Id.* at 7.

72. See *id.* at 7–8.

73. See *id.* at 7.

74. *Id.* at 7–8.

75. *Id.* at 8–10.

76. *Id.* at 8.

high—by 1947, PREPA alone had a total outstanding indebtedness of \$50 million.<sup>77</sup>

After World War II, more autonomy was given to the island (now deemed a Commonwealth, rather than merely a territory).<sup>78</sup> Growth in self-governance coincided with a growth in public debt. Consider that in 1953 the island's central government debt was pegged at \$33.1 million and then rose to \$144.3 million in 1960, with municipal debt going from \$105.2 million to \$313.7 million in the same period.<sup>79</sup> “[B]etween 1948 and 1960 total Puerto Rico public-sector debt rose by a factor of almost seven in nominal terms, while more than quintupling in real dollars.”<sup>80</sup> The island's leaders needed to pay for critical infrastructure, and capital markets were ready and all too willing to purchase Puerto Rico's attractive, triple-tax-exempt bonds. Between the 1960s and 1970s, central government debt jumped from \$144 million to \$1.6 billion, and public corporation debt spiked from \$314 million to \$5.2 billion.<sup>81</sup> Debt service requirements became so expensive that new debt was often issued just so that the government could meet the debt service payments due under existing debt.<sup>82</sup>

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77. *Id.*

78. *Id.* at 8–9

79. *See id.* at 9.

80. *Id.*

81. *Id.* at 14.

82. *See id.*; *see also* Nick Brown, *Puerto Rico's Debt Crisis Is Getting Deeper*, BUS. INSIDER (May 21, 2016, 4:00 PM), <http://www.businessinsider.com/puerto-ricos-debt-crisis-is-getting-deeper-2016-5>. These facts may make it seem like the island's government was irresponsible with the Commonwealth's borrowing capacity, and thus was entirely to blame. To some extent, politics and political corruption played a part in the crisis, but it would be an oversimplification to lay blame solely at the feet of malfeasant Puerto Rican politicians. Cut off from the mainland and treated (both from a policy and a legal perspective) as the neglected stepchild, Puerto Rico had been very much alone and adrift in dealing with its many serious economic challenges, including a decade-long recession. *See* JOFFE & MARTINEZ, *supra*, note 57, at 6; *see also* Nick Timiraos, *Puerto Rico's Debt Crisis in Seven Questions*, WALL ST. J.: REAL TIME ECON. (Apr. 13, 2016, 7:33 AM), <http://blogs.wsj.com/economics/2016/04/13/puerto-ricos-debt-crisis-in-seven-questions/>; *cf.* Joseph William Singer, *Tribal Sovereignty and Human Rights*, 2013 MICH. ST. L. REV. 307, 307–09 (discussing self-government in relation to human dignity and tribal sovereignty). Not only this, but the presence of multiple debt-issuing governmental entities is emblematic of the kind of defragmented government structure that leads to fiscal distress. *See* Clayton P. Gillette, *Dictatorships for Democracy: Takeovers of Financially Failed Cities*, 114 COLUM. L. REV. 1373, 1420–33 (2014). In Puerto Rico, union contracts were generous given the resources available to pay for them, and public sector jobs comprised a large percentage of employment. *See generally* *An Update on the Competitiveness of Puerto Rico's Economy*, FED. RESERVE BANK OF N.Y. (July 31, 2014), <https://www.newyorkfed.org/medialibrary/media/outreach-and-education/puerto-rico/2014/Puerto-Rico-Report-2014.pdf> (explaining how employment in the public sector has drastically decreased, which has created a very weak labor market). The result has been an exodus of

In 1976, Congress passed the Federal Tax Reform Act.<sup>83</sup> Among other things, this Act, specifically the famed section 936, allowed American manufacturers to “repatriate profits from Puerto Rico whenever they want[ed] to, free of U.S. [f]ederal taxes.”<sup>84</sup> Before the Act, if a U.S. company had a subsidiary on the island, it was subject to the regular corporation tax rate, plus a 15% withholding tax that was particular to Puerto Rico.<sup>85</sup> After the Act, no corporate taxes were owed, and Puerto Rico, to sweeten the deal, reduced their own rate to 10%.<sup>86</sup> Pharmaceutical companies, among other manufacturers—everyone from Microsoft to Star-Kist tuna<sup>87</sup>—saw this as a huge boon.<sup>88</sup>

But then, in 1996, Congress passed the Small Business Job Protection Act, which phased out section 936 (with its generous tax breaks for U.S. businesses operating in Puerto Rico), as a way to offset newly enacted federal tax breaks on the mainland and to counterbalance a rise in the federal minimum wage.<sup>89</sup> By January 2006, the tax break was completely eliminated.<sup>90</sup> This event kicked off a recession on the island, which has persisted until present day.<sup>91</sup> After the repeal, manufacturers closed up shop almost

residents who might otherwise contribute to productive capacity. *See id.* Thus, poor institutional design played as large a role as any. *See* Clayton P. Gillette & David A. Skeel, Jr., *Governance Reform and the Judicial Role in Municipal Bankruptcy*, 125 *YALE L.J.* 1150, 1152–53 (2016).

83. A. Lin Neumann, *U.S. Pharmaceutical Giants Move to Puerto Rico for Tax Breaks*, 2 *MULTINATIONAL MONITOR*, Oct. 1981, <http://www.multinationalmonitor.org/hyper/issues/1981/10/neumann.html>.

84. *Id.*

85. *Id.*

86. *Id.*

87. Larry Luxner, *New US Law Marks the End of an Era for Puerto Rico*, *LUXNER NEWS INC.* (Sept. 16, 1996), [http://www.luxner.com/cgi-bin/view\\_article.cgi?articleID=833](http://www.luxner.com/cgi-bin/view_article.cgi?articleID=833).

88. *See* Neumann, *supra* note 83. For the first five years of operation on the island, these companies received a 90% income and property tax break, which was reduced to the still-significant number of 75% thereafter. *Id.* Furthermore, all American companies on the island were entitled to a full exemption from all municipal taxes. *See id.* The economic benefits of operating on the island were immense. For instance, in 1977 the company Schering-Plough “recorded 67% of its worldwide earnings in Puerto Rico; Abbott 71%; Lilly and Merck each recorded more than 20%.” *Id.* But unfortunately, these tax breaks provided little benefit in return. One economist noted that the pharmaceutical companies “buy labor, utilize the infrastructure and make use of government subsidies. That’s it.” *Id.* Although the pharmaceutical industry accounted for 32% of the Commonwealth’s GDP, only 7% of the island’s manufacturing sector workforce was employed in the pharmaceutical industry. *Id.* Indeed, despite the generous business incentives, the island maintained a 15% unemployment rate (triple that of the United States by the 1990s). Luxner, *supra* note 87.

89. Luxner, *supra* note 87.

90. *Id.*

91. *See* Greenberg & Ekins, *supra* note 62.

immediately—nearly sixty-one companies shut down.<sup>92</sup> By November 1996, the manufacturing sector lost a net of 17,720 jobs, bringing the total number of jobs to the lowest in two decades.<sup>93</sup>

Over time, things have not gotten better for the financial state of the island. Thanks in no small part to strong support from Wall Street,<sup>94</sup> Puerto Rico's current total debt burden is a shocking \$72 billion (larger than any state aside from New York and California).<sup>95</sup> Major credit rating agencies like Standard & Poor's and Moody's have downgraded the island's bonds to junk status.<sup>96</sup> The unemployment rate hovers at 15.4% (triple that of the United States average), and the cost of living has risen sharply.<sup>97</sup> Coupled with a rising crime rate resulting from economic unrest and the exodus of doctors, accountants, lawyers, trained professionals, and many upper-class and middle-class Puerto Ricans, the crisis has sent the Commonwealth into a downward spiral.<sup>98</sup> The poverty rate on the

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92. Ivan Roman, *Puerto Ricans Scramble for Jobs as Plants Close*, ORLANDO SENTINEL (Oct. 17, 1999), [http://articles.orlandosentinel.com/1999-10-17/news/9910150370\\_1\\_puerto-rico-section-936-manufacturing](http://articles.orlandosentinel.com/1999-10-17/news/9910150370_1_puerto-rico-section-936-manufacturing).

93. *Id.* For perspective, consider that during that same one-year period Puerto Rico's manufacturing sector saw a decline of 5%, with the U.S. national average decline being only 1.25%. *Id.*

94. Wall Street made sure to profit from the island's vulnerable fiscal position. See Bill Faries et al., *How Wall Street Fed Puerto Rico's \$70 Billion Debt Binge*, BLOOMBERG, <http://www.bloomberg.com/news/articles/2013-10-22/how-wall-street-fed-puerto-rico-s-70-billion-borrowing-binge> (last updated Oct. 22, 2013, 11:26 AM). Since 2000, major financial firms and investment banks have garnered almost \$900 million in fees in connection with Puerto Rico's various bond issuances. *Id.* "Citigroup Inc. and its Salomon Smith Barney unit were Puerto Rico's top bankers, managing \$27 billion of issues, while [United Bank of Switzerland] was second, with \$25.6 billion, data show." *Id.* Moreover, Wall Street has been able to take advantage of Puerto Rico's financial situation in a way that it was not able to do with other failing governmental entities. See Jake Zamansky, *How Wall Street Has Profited from Puerto Rico's Misery*, FORBES (Nov. 13, 2013, 10:27 AM), <http://www.forbes.com/sites/jakezamansky/2013/11/13/how-wall-street-has-profited-from-puerto-ricos-misery-2/#456d98a84663>. Of a total of eighty-seven Puerto Rican bond transactions that occurred in 2006 totaling \$61 billion, investment banks raked in \$1.4 billion in fees. *Id.* The actual fee percentages charged to the island's issuers were higher than those typically charged to financially distressed American cities. *Id.* In fact, "banks such as [the United Bank of Switzerland], were paid gross spreads averaging 31% higher than spreads charged to Detroit." *Id.* For a historical perspective on Wall Street's involvement in pre-Great Depression municipal crises, see A.M. HILLHOUSE, *MUNICIPAL BONDS: A CENTURY OF EXPERIENCE* (1936).

95. Michelle Kaske & Martin Z. Braun, *Puerto Rico's Slide*, BLOOMBERG, QUICKTAKE, <https://www.bloomberg.com/quicktake/puerto-ricos-slide> (last updated Nov. 18, 2016, 9:16 PM).

96. Lizette Alvarez, *Economy and Crime Spur New Puerto Rican Exodus*, N.Y. TIMES (Feb. 8, 2014), [http://www.nytimes.com/2014/02/09/us/economy-and-crime-spur-new-puerto-rican-exodus.html?\\_r=0](http://www.nytimes.com/2014/02/09/us/economy-and-crime-spur-new-puerto-rican-exodus.html?_r=0).

97. *Id.*

98. *See id.*

island is now double that of Mississippi—the most impoverished state in the United States.<sup>99</sup>

As investors have tried to off-load Puerto Rican debt, certain hedge funds that are known for purchasing low-grade debt (often called vulture funds) have swept in and acquired a sizable chunk of the island's bonded indebtedness at deep discounts.<sup>100</sup> Some of the discounts range from 30% to 50% of the bond's par value.<sup>101</sup>

As things came to a head, in July 2015, the Commonwealth's governor declared on live television that the island could not pay its \$72 billion in debt—there simply was “no more cash.”<sup>102</sup> Being that Puerto Rico is unable to utilize the federal bankruptcy laws in the way that Detroit, Stockton, and others have,<sup>103</sup> Congress decided to

99. Kaske & Braun, *supra* note 95.

100. Michael Corkery & Mike Cherney, *Banks Rack Up Big Fees From Puerto Rico Bond Deals*, WALL ST. J. (Oct. 22, 2016, 9:40 PM), <http://www.wsj.com/news/articles/SB10001424052702303672404579151703348313062>; see also Bill Faries, *Summers Sees Low Market Confidence in Puerto Rico Bonds*, BLOOMBERG (Nov. 7, 2013, 12:48 PM), <http://www.bloomberg.com/news/articles/2013-11-07/summers-sees-low-market-confidence-in-puerto-rico-bonds>.

101. Corkery & Cherney, *supra* note 100.

102. Rashid Marcano-Rivera, *Puerto Rico Can't Pay Its Debt, and the United States Is Partly to Blame*, WASH. POST, MONKEY CAGE BLOG (July 15, 2015), <https://www.washingtonpost.com/blogs/monkey-cage/wp/2015/07/15/puerto-rico-cant-pay-its-debt-and-the-united-states-is-partly-to-blame/>. As will be discussed in Subart II.B, part of this amount is Commonwealth debt and part is political subdivision debt. Even under Chapter 9 of the Bankruptcy Code, state-level (or what we might say in this case—Commonwealth-level) debt cannot be put through insolvency proceedings. Only the debt of Puerto Rico's public corporations would qualify.

103. For reasons that are a complete mystery, Puerto Rico is cut off from the protection and benefits of the federal bankruptcy laws. Mary Williams Walsh, *Puerto Rico Fights for Chapter 9 Bankruptcy in Supreme Court*, N.Y. TIMES, DEALBOOK (Mar. 22, 2016), [http://www.nytimes.com/2016/03/23/business/dealbook/puerto-rico-fights-for-chapter-9-bankruptcy-in-supreme-court.html?\\_r=0](http://www.nytimes.com/2016/03/23/business/dealbook/puerto-rico-fights-for-chapter-9-bankruptcy-in-supreme-court.html?_r=0). In 1898, Congress enacted the Bankruptcy Act and explicitly stated that territories of the United States (specifically incorporating Puerto Rico) were included in the definition of “state” for purposes of the statute. Stephen Mihm, Opinion, *Congress Goofed. Puerto Rico Pays.*, BLOOMBERGVIEW (Dec. 3, 2015, 12:34 PM), <http://www.bloomberg.com/view/articles/2015-12-03/bankruptcy-was-option-for-puerto-rico-before-congress-goof>. Then, in 1934 (and later in 1937), Congress passed the Municipal Bankruptcy Act that granted to municipalities and related public corporations the ability to seek bankruptcy protection, provided they received permission of their “state.” See *id.* This law was later updated and revised in 1978, along with the entire Bankruptcy Code, with the introduction of Chapter 9 that granted protections to “a political subdivision or public agency or instrumentality of a State.” *Id.* Unfortunately, with this revision came a neglect to define the word “state.” *Id.* There was an immediate move the very next year to fix this problem by including in the definition of “state,” among other locales, the Commonwealth of Puerto Rico and the District of Columbia. Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, § 421, 98 Stat. 333, <https://www.govtrack.us/congress/bills/98/hr5174/text>. The “fix” bill passed the

Senate and then moved on to the House of Representatives. For reasons that are completely a mystery (despite having been investigated extensively lately) the bill was amended to clarify that the word “state” included D.C. and Puerto Rico for all Bankruptcy Code purposes, *except for those involving the ability to utilize Chapter 9*. Jon Greenberg, *PolitiFact: Strom Thurmond’s Intent in Puerto Rico Bankruptcy Protection Is Murky*, TAMPA BAY TIMES (Apr. 28, 2016, 8:41 PM), <http://www.tampabay.com/news/politics/politifact-strom-thurmonds-intent-in-puerto-rico-bankruptcy-protection-is/2275210>. As a result of this change, Puerto Rico was seemingly brought under the ambit of the Bankruptcy Code, yet simultaneously its municipalities and public corporations were cut off from the bankruptcy process. See Mihm, *supra*. The “fix” legislation was ultimately tossed into a much larger Act (called the Bankruptcy Amendments and Federal Judgeship Act) and was finally passed. *Id.* Puerto Rico was completely cut off from Chapter 9 bankruptcy and remains so today. The reason remains a complete and utter mystery.

Unable to avail itself of federal bankruptcy protection, the government of Puerto Rico decided to take matters into its own hands. In March 2014, the legislature passed the Puerto Rico Public Corporation Debt Enforcement and Recovery Act (“Recovery Act”). Government Development Bank for Puerto Rico, *The Facts About Puerto Rico’s Public Corporations: Debt Enforcement and Recovery Act*, <http://www.bgfpr.com/documents/FactsAboutDebtEnforcementAndRecoveryAct.pdf> (last visited Nov. 26, 2016). This law essentially created a mini-bankruptcy-like process for the island’s public corporations to deal with their debt, mimicking many of the attributes of Chapter 9. See *id.* It allows public corporations on the island a means by which to restructure their crippling debt. *Id.* This move was not met with welcome arms by the island’s bondholders. Tim McLaughlin, *U.S. Bond Funds Sue Puerto Rico, Worried About Bankruptcy Threat*, REUTERS (June 30, 2014, 12:04 PM), <http://www.reuters.com/article/us-puertorico-funds-bonds-idUSKBN0F51J420140630>. A group of them quickly filed a lawsuit in late summer 2014, arguing that the Recovery Act was unconstitutional because it was preempted by the Bankruptcy Code. *Franklin Cal. Tax-Free Tr. v. Puerto Rico*, 805 F.3d 322, 324 (1st Cir. 2015), *aff’d*, 136 S. Ct. 1938 (2016). The theory was that, in enacting the Bankruptcy Code, Congress has precluded state or other lower-level governments from passing laws relative to insolvency regimes. Jack Casey, *Supreme Court to Review Ruling on Puerto Rico Restructuring Law*, BOND BUYER (Dec. 4, 2015), <http://www.bondbuyer.com/news/washington-budget-finance/supreme-court-to-review-ruling-on-puerto-rico-restructuring-law-1091087-1.html>. Since Chapter 9 of the Bankruptcy Code provides for insolvency proceedings for local governments and municipalities of states, and Puerto Rico is defined in the Code as a “state,” then Puerto Rico is not free to create its own version of Chapter 9. See *id.* The federal district court and the First Circuit agreed with this theory and struck down the Recovery Act (albeit accompanied by a vigorous concurrence on behalf of the island by Judge Torruella, one of the Commonwealth’s native sons and the only Puerto Rican to sit on the federal appeals court that oversees the island). See *Franklin Cal. Tax-Free Tr.*, 85 F. Supp. 3d 577 (D. P.R. 2015); *Franklin Cal. Tax-Free Tr.*, 805 F.3d 322 (1st Cir. 2015). Puerto Rico appealed to the Supreme Court. *Franklin Cal. Tax-Free Tr.*, 805 F.3d at 355 (Torruella, J., concurring) (“The majority’s disregard for the arbitrary and unreasonable nature of the legislation enacted in the 1984 Amendments showcases again this court’s approval of a relationship under which Puerto Rico lacks any national political representation . . . This is clearly a colonial relationship, one which violates our Constitution and the Law of the Land as established in ratified treaties. Given the vulnerability of these

take up the cause of the island's debt crisis.<sup>104</sup> The Natural Resources Committee in the House of Representatives, at the request of Speaker Paul Ryan,<sup>105</sup> put forth PROMESA.<sup>106</sup> After much Congressional haggling, the bill was signed by the President the day before the island made a \$2 billion default.<sup>107</sup>

The content of PROMESA is not necessarily important for purposes of this Article. Suffice it to say that, although not federal bankruptcy law itself, the bill incorporates many provisions of Title 11 of the United States Code.<sup>108</sup> For instance, the Federal Rules of Bankruptcy Procedure apply, and familiar concepts such as the "automatic stay, financing, majority voting rules, cram down, discharge, and the discharge injunction" apply.<sup>109</sup> The actual process of restructuring the debt would be directed by an oversight board, but the case would be handled by a federal district court judge appointed by the Chief Justice of the Supreme Court of the United States.<sup>110</sup> The subject of much criticism, the oversight board must have an office in Puerto Rico and one in D.C., although the actual location of the federal district court is up in the air, and the

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citizens before the political branches of government, it is a special duty of the courts of the United States to be watchful in their defense.").

On June 13, 2016, the Supreme Court released its ruling in *Puerto Rico v. California Tax-Free Trust*, 136 S. Ct. 1938 (2016), and struck down the island's Recovery Act as being unconstitutional based on the preemptive effect of the U.S. Bankruptcy Code—thereby taking away another tool for the island to deal with its debt crisis. *Id.* at 1942.

104. Vann R. Newkirk II, *Congress's Promise to Puerto Rico*, ATLANTIC (May 19, 2016), <http://www.theatlantic.com/politics/archive/2016/05/congress-puerto-rico-bill-promise/483572/>.

105. Mary Clare Jalonick, *House Speaker Paul Ryan Says Congress Needs to "Bring Order to the Chaos" in Puerto Rico and Prevent American Taxpayers from Having to Eventually Bail out the Territory, Which Is Facing \$70 billion in Debt*, U.S. NEWS (Apr. 14, 2016, 6:36 PM), <http://www.usnews.com/news/business/articles/2016-04-14/puerto-rico-faces-defaults-as-congress-stalls-on-way-to-help>.

106. Puerto Rico Oversight, Management, and Economic Stability Act, Pub. L. No. 114-187, 130 Stat. 549 (2016), <https://www.congress.gov/bill/114th-congress/senate-bill/2328/text?q=%7B%22search%22%3A%5B%22promesa%22%5D%7D&resultIndex=1#toc-HF900DD8D7E5F41AA9F4DB7AE83FDF2CD>.

107. Osita Nwanevu, *Obama Just Signed a Controversial Puerto Rico Debt Plan into Law*, SLATE (June 30, 2016, 5:07 PM), [http://www.slate.com/blogs/the\\_slatest/2016/06/30/obama\\_signs\\_puerto\\_rico\\_debt\\_plan\\_into\\_law.html](http://www.slate.com/blogs/the_slatest/2016/06/30/obama_signs_puerto_rico_debt_plan_into_law.html).

108. See Melissa Jacoby, *Puerto Rico: PROMESAankruptcy*, CREDIT SLIPS (Mar. 30, 2016, 7:47 PM), <http://www.creditslips.org/creditslips/2016/03/puerto-rico-promesa.html>.

109. See *id.*

110. *Id.*; see also Melissa Jacoby, *Puerto Rico: PROMESA and Presiding Judges*, CREDIT SLIPS (May 26, 2016, 1:32 PM), <http://www.creditslips.org/creditslips/2016/05/puerto-rico-presiding-over-promesankruptcy.html> (pointing out the strange situation of having a federal district court judge, one with little to no bankruptcy experience, preside over a complex, bankruptcy-like insolvency proceeding).

board would have the practical effect of displacing the governing powers of the Commonwealth's elected decision makers.<sup>111</sup> As of this writing, the mechanics of the debt recomposition process—as well as who will be appointed to serve on the oversight board—remain to be seen.

### B. *The Unrecognized Reconciliation of Rights*

The contemporary framing of the Puerto Rican financial crisis centers on the juxtaposition of two opposing sides.<sup>112</sup> As noted above, a number of bondholders invoke claims to property and arguments about the importance of stability and predictability in the marketplace as signature reasons for pushing back against the passage of PROMESA.<sup>113</sup> Indeed, in the complaint challenging the constitutionality of the island's earlier attempt at a debt restructuring, the numerous plaintiff investment funds made property rights claims under the Fifth Amendment.<sup>114</sup> Even the rhetoric advanced by the creditors and their surrogates point to property-based claims: one commentator warned that the debt restructuring plan currently being considered by Congress “threatens to disregard property rights in favor of a nostrum—one that will help make Puerto Rico's debt death spiral perpetual.”<sup>115</sup> Others have noted that forcing a restructuring on the investors undermines “fidelity to the rule of law and property rights.”<sup>116</sup> Political ads warn of “retirement accounts crushed, a bailout on the backs of savers and seniors,” all amounting to allowing the government of the island to “take” from others without consequence or care.<sup>117</sup>

As for the government and people of Puerto Rico, their defense is not based in pure property rights—at least not as traditionally conceived<sup>118</sup>—but rather in relation to the humanitarian crisis

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111. See Jacoby, *supra* note 108.

112. Logan Beirne, Opinion, *Why Puerto Rico's Super Restructuring Is Bad Policy*, HILL, CONGRESS BLOG (Apr. 2, 2016, 8:19 AM), <http://thehill.com/blogs/congress-blog/economy-budget/274964-why-puerto-ricos-super-restructuring-is-bad-policy>.

113. Ctr. for Individual Freedom Staff, *Congress's Role in Puerto Rico's Debt Crisis*, CTR. FOR INDIVIDUAL FREEDOM (May 3, 2016), <http://cfif.org/v/index.php/commentary/54-state-of-affairs/3084-congresss-role-in-puerto-ricos-debt-crisis>.

114. See Complaint at 14, *Franklin Cal. Tax-Free Tr. v. Puerto Rico*, 805 F.3d 322 (1st Cir. 2015) (No. 14-1518) (“The operation of the Act, as enacted by the Commonwealth and signed [or soon to be signed] into law by the Governor, threatens to improperly impair Plaintiffs' rights under the PREPA Bonds in contravention to the Bankruptcy Clause, the Takings Clause, and the Contract Clause.”).

115. Beirne, *supra* note 112.

116. Ctr. for Individual Freedom Staff, *supra* note 113.

117. Ctr. for Individual Freedom, *supra* note 32.

118. The traditional and long dominant view of property rights is based on the idea of exclusion and the authority and dominion of the individual over the

unfolding on the island. The governor of Puerto Rico reports having to decide between paying the island's creditors or cutting fire, police, and other essential social services.<sup>119</sup> Advocates for the island focus on the human toll that the crisis has caused, including "drastic spending cuts and tax hikes" as well as the laying off of large numbers of public-sector workers.<sup>120</sup> Supporters of the Commonwealth testifying before Congress on relief legislation state that "this is not a debt crisis, but a humanitarian crisis," noting that nearly 50% of the islanders live in poverty.<sup>121</sup> They note that self-imposed austerity is harming children, compromising public safety, and decimating the island's public health system.<sup>122</sup> The human stories of the people of Puerto Rico should and must, so they argue, justify a yielding of the property claims of the bondholders.

But, in truth, both sides of this debate miss the mark—both their arguments are wrongheaded. They assume that bondholders have no human dignity interests and, conversely, that the Puerto Rican people have no property rights at stake. This view fails to understand that a more progressive account of property law teaches that human values lead us to define property rights in situations where the protection of private rights will cause human suffering. The following Subparts show that both sides have legitimate claims to human dignity and property rights in the Commonwealth's debt crisis, as suggested by the progressive property literature.

### 1. *Human Rights and Social Property in the Commonwealth*

The human rights narrative, as a counter to the property narrative, does not appreciate the ways in which the concept of property embraces the notions of human dignity. As members of the

thing. See Robert E. Ellickson, *Property in Land*, 102 YALE L.J. 1315, 1327–28 (1993); Thomas W. Merrill & Henry E. Smith, *The Morality of Property*, 48 WM. & MARY L. REV. 1849, 1853–54 (2007); Thomas W. Merrill & Henry E. Smith, *Optimal Standardization in the Law of Property: The Numerus Clausus Principle*, 110 YALE L.J. 1, 23–24 (2000); Thomas W. Merrill, *Property and the Right to Exclude*, 77 NEB. L. REV. 730, 731 (1998); Thomas W. Merrill & Henry E. Smith, *The Property/Contract Interface*, 101 COLUM. L. REV. 773, 790 (2001); Thomas W. Merrill & Henry E. Smith, *What Happened to Property in Law and Economics?*, 111 YALE L.J. 357, 360–61 (2001); Henry E. Smith, *Exclusion Versus Governance: Two Strategies for Delineating Property Rights*, 31 J. LEGAL STUD. S453, S455 (2002). See generally THOMAS W. MERRILL & HENRY E. SMITH, *PROPERTY: PRINCIPLES AND POLICIES* (Foundation Press 2d ed. 2012).

119. CNN, *supra* note 43.

120. Daniel Marans, *5 Things You Should Know as Puerto Rico Confronts Its Unpayable Debt*, HUFFINGTON POST (Apr. 28, 2016, 9:11 PM), [http://www.huffingtonpost.com/entry/puerto-rico-debt-crisis-may-deadline\\_us\\_57228dc8e4b0f309baf06905](http://www.huffingtonpost.com/entry/puerto-rico-debt-crisis-may-deadline_us_57228dc8e4b0f309baf06905).

121. Jubilee USA, *Eric LeCompte Testifies to Congress on Puerto Rico Humanitarian Crisis*, YOUTUBE (Feb. 12, 2016), <https://www.youtube.com/watch?v=nWiz-5fT3sI>.

122. *Id.*

progressive property movement so forcefully note, property law is not only “individual” based, but rather is also “social in nature.”<sup>123</sup> Thus, property rights should be viewed not necessarily through the lens of efficiency or utility, but rather in a way that considers “socially-oriented politics and deep moral considerations that attend not only to the interests of owners but to the interests of nonowners, unborn generations, and the larger ecological community of which humans are a part.”<sup>124</sup>

Under this theory, the humanitarian concerns of the Puerto Ricans are deeply tied to property rights—their own property rights. Professors Hanri Morsert and Thomas Bennett posit that “the only legitimate reason for the existence of property rights is their contribution to human well-being.”<sup>125</sup> Therefore, the allocation and protection of property rights are not merely a matter for the creditors. Rather, the people of Puerto Rico, facing a severe humanitarian crisis, also have a property-related stake.<sup>126</sup> This stake finds its origins in the notion that private property has a role to play in human flourishing—which includes, among other things, the need for food to survive, “shelter from the elements[,] and physical places where humans can live, thrive, and enjoy privacy.”<sup>127</sup> I refer to the claim that property rights and human dignity concerns are deeply interwoven as a claim to “social property.” The following discussion puts social property claims into focus from the perspective of the Puerto Ricans.

Consider first the social property aspects of public health in Puerto Rico. The island is suffering from a dearth of medical professionals.<sup>128</sup> By one account, in the period between 2014 and

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123. Gregory Alexander et al., *A Statement of Progressive Property*, 94 CORNELL L. REV. 743, 744 (2009); Gregory Alexander, *Ownership and Obligations: The Human Flourishing Theory of Property*, 43 HONG KONG L.J. 451, 458 (2013); Joseph William Singer, *Property and Social Relations*, in PROPERTY AND VALUES 3, 11–12 (Charles Geisler & Gail Daneker eds., 2000).

124. See Timothy M. Mulvaney, *Progressive Property Moving Forward*, 5 CAL. L. REV. CIR. 349, 352 (2014).

125. Eric T. Freyfogle, *Private Ownership and Human Flourishing: An Exploratory Overview*, 24 STELLENBOSCH L. REV. 430, 430 (2013) (citing Thomas Bennett & Hanri Mostert, *Access to Property in Africa*, in PLURALISM AND DEVELOPMENT 1, 5 (Hanri Mostert & Thomas Bennett eds., 2011)).

126. *Addressing Puerto Rico's Economic and Fiscal Crisis and Creating a Path to Recovery: Roadmap for Congressional Action*, WHITE HOUSE 1, 1–2, [https://www.whitehouse.gov/sites/default/files/roadmap\\_for\\_congressional\\_action\\_puerto\\_rico\\_final.pdf](https://www.whitehouse.gov/sites/default/files/roadmap_for_congressional_action_puerto_rico_final.pdf) (last visited Nov. 26, 2016); The Week Staff, *Everything You Need to Know About the Puerto Rico Debt Crisis*, FISCAL TIMES (Mar. 29, 2016), <http://www.thefiscaltimes.com/2016/03/29/Everything-You-Need-Know-About-Puerto-Rico-Debt-Crisis>.

127. See Freyfogle, *supra* note 125, at 432.

128. Heather Long, *Puerto Rico is Losing a Doctor a Day*, CNN MONEY (Apr. 13, 2016, 12:01 PM), <http://money.cnn.com/2016/04/13/investing/puerto-rico-debt-medicare/>; PBS NewsHour, *Amid New Austerity, A Push to Restructure*

2015, the Commonwealth lost 864 doctors—many with needed specialties.<sup>129</sup> For instance, “only 90 obstetricians are left to handle an average of 34,000 births annually.”<sup>130</sup> This outmigration of medical professionals is particularly important because 1.6 million Puerto Ricans (a third of the people on the island) rely on the Commonwealth’s Medicaid program for their healthcare.<sup>131</sup>

To put a human face on these figures, consider the emergency room of San Juan’s most important healthcare facility—Centro Medico Hospital.<sup>132</sup> Patients line the halls because there are not enough nurses to treat them or rooms to house them.<sup>133</sup> Patients usually wait in the hall several days to a week to get a room.<sup>134</sup> Also, higher sales taxes (raised to help manage the debt) are costing hospitals more for everything they have to purchase.<sup>135</sup> According to one executive for Ashford Presbyterian Hospital, the increase in sales taxes will result in a rise of \$700,000 in the overall cost of purchasing the items needed to operate the hospital.<sup>136</sup>

Moreover, the island’s healthcare outcomes are abysmal.<sup>137</sup> Puerto Ricans have the highest national prevalence of diabetes and hypertension, among other diseases.<sup>138</sup> Children on the island have the highest pediatric asthma rates in the United States and one of the highest premature birth rates in the world.<sup>139</sup> To make matters worse, an even more acute public health crisis has arisen—as of June 2016, over one thousand Puerto Ricans were infected with the

*Puerto Rico’s Debt*, YOUTUBE (Aug. 22, 2015), <https://www.youtube.com/watch?v=ziuw1TtO9oM>.

129. Gretchen Sierra-Zorita, Opinion, *Puerto Rico’s Unseen Crisis*, CNN, <http://www.cnn.com/2016/05/10/opinions/puerto-rico-health-crisis-gretchen-sierra-zorita/> (last updated May 10, 2016, 5:26 PM).

130. *Id.*

131. David Thomsen, *Healthcare Funding Gaps Deepen Humanitarian Crisis in Puerto Rico*, NCLRBLOG (Dec. 7, 2015), <http://blog.nclr.org/2015/12/07/healthcare-funding-gaps-deepen-humanitarian-crisis-in-puerto-rico/>.

Although the people of Puerto Rico pay the same amount into the Medicaid system as those living on the U.S. mainland, the federal government only funds 15 to 20% of the island’s healthcare expenses (compared to the 50 to 83% funded on the mainland). Thus, the cost of making up the difference falls on the perpetually struggling Puerto Rican legislature—a task it is hardly situated to accomplish in the government’s current financial state. *Id.*

132. PBS NewsHour, *supra* note 128.

133. *Id.*

134. *Id.*

135. *Id.*

136. *Id.*

137. Maria Levis, *The Price of Inequality for Puerto Rico*, HEALTH AFFAIRS BLOG (Dec. 29, 2015), <http://healthaffairs.org/blog/2015/12/29/the-price-of-inequality-for-puerto-rico/>.

138. *Id.*

139. *Id.*

Zika virus.<sup>140</sup> The virus, which is mosquito-borne and causes severe birth defects, is a source of major concern for Commonwealth leaders.<sup>141</sup> The Centers for Disease Control and Prevention predicted that eventually one-quarter of the island will be infected,<sup>142</sup> and the island's governor has even publically requested that people refrain from getting pregnant due the inability of the country's healthcare system to deal with the epidemic.<sup>143</sup> A flourishing account of property necessarily embraces human health—the right of the Puerto Ricans to minimum standards of care so that they may live freely and prosper—and forms but one of the island's social property claims.

Access to a basic education is also part of the claim to social property, and the island's educational system is very much in distress. Students at various campuses at the University of Puerto Rico have started striking in the face of major austerity cuts to higher education.<sup>144</sup> The university has taken a severe hit financially, which has resulted in many students not being able to complete their degrees, often when the students are in the middle of enrollment.<sup>145</sup> At the eleven campuses of the University of Puerto Rico, a tremendous number of professors have been laid-off, and a large number of academic programs closed, leaving many students with nowhere to go.<sup>146</sup>

Cuts to elementary and secondary education have been even worse. More than 150 schools have been shut down in the past few years.<sup>147</sup> Take for instance Francisco Oller Elementary School in

140. Marissa Evans, *Puerto Rico Zika Outbreak Highlights Island's Medicaid Woes*, ROLL CALL (June 2, 2016, 4:46 PM), <http://www.rollcall.com/news/policy/puerto-rico-zika-outbreak-highlights-islands-medicaid-woes#sthash.QRvhVX0g.dpuf>.

141. Sierra-Zorita, *supra* note 129. In early May 2016, two sports teams—the Pittsburgh Pirates and the Miami Marlins—cancelled a two-game series that was to take place on the island because of concerns related to the Zika virus. Jonathan Miller, *Zika Scares Major League Baseball Out of Puerto Rico*, ROLL CALL (May 6, 2016, 7:15 PM), <http://www.rollcall.com/news/policy/zika-scares-major-league-baseball-puerto-rico>.

142. Donald G. McNeil, Jr., *Puerto Rico Braces for Its Own Zika Epidemic*, N.Y. TIMES (Mar. 19, 2016), [http://www.nytimes.com/2016/03/20/health/zika-virus-puerto-rico.html?\\_r=0](http://www.nytimes.com/2016/03/20/health/zika-virus-puerto-rico.html?_r=0).

143. Sierra-Zorita, *supra* note 129.

144. *University of Puerto Rico Students Vote to Shut Down Campus over Austerity Cuts*, DEMOCRACYNOW! (Mar. 16, 2016), [http://www.democracynow.org/2016/3/16/headlines/university\\_of\\_puerto\\_rico\\_students\\_vote\\_to\\_shut\\_down\\_campus\\_over\\_austerity\\_cuts](http://www.democracynow.org/2016/3/16/headlines/university_of_puerto_rico_students_vote_to_shut_down_campus_over_austerity_cuts).

145. *Special Report: Voices from Puerto Rico's Students Leading an Anti-Austerity Movement*, DEMOCRACY NOW! (Apr. 6, 2016), [http://www.democracynow.org/2016/4/6/special\\_report\\_voices\\_from\\_puerto\\_rico](http://www.democracynow.org/2016/4/6/special_report_voices_from_puerto_rico).

146. *Id.*

147. Danica Coto, *Wave of Public School Closures in Puerto Rico Highlights Deepening Economic Crisis*, FOX NEWS WORLD (May 14, 2015),

San Juan.<sup>148</sup> The building once bustled with children, “but now birds nest in classrooms strewn with leaves and glass from shattered fluorescent lights. . . Graffiti covers the walls.”<sup>149</sup> Government leaders warn that over the course of the next several years “it may have to close nearly 600” more schools out of the island’s remaining 1387.<sup>150</sup>

A number of these closed and now abandoned schools have become a haven for drug trafficking and are a major safety concern for the surrounding neighborhoods.<sup>151</sup> In a recent visit to Puerto Rico by U.S. Treasury Secretary Jacob Lew in May 2016, a fourth grade teacher pointed out that her classroom had only one outlet and that “running multiple devices—such as a television, air conditioner, or a fan—would trip the breaker and that multiple classrooms using electricity together would cause the whole building’s power to fail.”<sup>152</sup> The teacher also drew the dignitary’s attention “to the cracks in the wall and the broken fans in the room, which already sweltered in early May as the humidity settled in like a blanket over an 83-degree day.”<sup>153</sup> Special needs children at one particular school visited by the secretary were taught in trailers that had limited access to power.<sup>154</sup> The plight of these children and the broader state of the educational system of the Commonwealth are both deeply tied to the social property claims of its people—claims to a basic education and the chance to flourish.

So typical of local governments facing insolvency, the workforce and the broader Puerto Rican economy have also been hit hard.<sup>155</sup> Many shops and businesses in the capital of San Juan and in other cities throughout the island have been closed as a result.<sup>156</sup> Over thirty thousand public sector workers were laid off in 2009.<sup>157</sup>

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<http://www.foxnews.com/world/2015/05/14/wave-public-school-closures-in-puerto-rico-highlights-deepening-economic-crisis.html>.

148. *Id.*

149. *Id.*

150. *Id.*

151. *See id.*

152. Vann R. Newkirk II, *supra* note 40.

153. *Id.*

154. *Id.*

155. Judy Woodruff, *Puerto Rican Economic Disaster Leaves Residents Struggling*, PBS NEWS HOUR (May 6, 2016, 7:40 PM), <http://www.pbs.org/newshour/bb/puerto-rican-economic-disaster-leaves-residents-struggling/>.

156. Danica Coto, *Misery Is Deepening in Puerto Rico*, BUS. INSIDER (Aug. 3, 2015, 6:50 AM), <http://www.businessinsider.com/misery-is-deepening-in-puerto-rico-2015-8>.

157. Associated Press, *Puerto Rico Gov.: 30,000 Workers Could Be Fired Amid Crisis*, DAILY NEWS (Mar. 4, 2009, 4:44 PM), <http://www.nydailynews.com/latino/puerto-rico-gov-30-000-workers-fired-crisis-article-1.369458>; *Puerto Rican Government Launches Controversial Round of Layoffs*, LATIN AM. HERALD TRIB., <http://www.laht.com/article.asp?CategoryId=14092&ArticleId=336085> (last visited Nov. 26, 2016).

Official unemployment is at 12.5%.<sup>158</sup> Good, economy-growing jobs have disappeared as austerity measures have been imposed, leaving only temporary, part-time, and low-wage work.<sup>159</sup> In one account, a man living in San Juan's poorest neighborhood fixing cars reported working eighty hours a week in order to pay for the rising costs of basic living essentials.<sup>160</sup> "Water and electricity bills are three times the price of those in the 50 states, sales taxes the highest in the nation."<sup>161</sup>

Aside from a weak labor market, jurisdictions facing insolvency typically face challenges related to blight.<sup>162</sup> Puerto Rico is no different. The island is filled with abandoned cities and towns, fast on the decline.<sup>163</sup> Towns like Arecibo, once a vibrant commercial center from the sugar cane industry, is now a ghost town with shut-down schools and boarded up windows and buildings everywhere.<sup>164</sup> In order to meet continuing debt obligations, even harsher austerity plans have been or are being proposed.<sup>165</sup> The rights of workers, including employee benefits, are being cut, and there is talk of the minimum wage being scrapped as well—with some suggesting that the island should be allowed to go below the federal minimum wage in order to be competitive with other neighboring, non-U.S. islands.<sup>166</sup> These broader economic and labor interests have deep

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158. Teddy Shibabaw, *Puerto Rico—A Spiraling Crisis of Debt, Austerity, and Colonialism*, SOCIALIST ALTERNATIVE (Feb. 29, 2016), [http://www.socialistalternative.org/2016/02/29/puerto\\_rico\\_austerity/](http://www.socialistalternative.org/2016/02/29/puerto_rico_austerity/).

159. *See id.*

160. Meredith Hoffman, *Puerto Rico's Debt Crisis Empties Houses, Impoverishes Citizens*, VICE NEWS (Feb. 3, 2016, 4:25 PM), <https://news.vice.com/article/puerto-ricos-debt-crisis-empties-houses-impoverishes-citizens>.

161. *See id.*

162. *See* Michelle W. Anderson, *The New Minimal Cities*, 123 YALE L.J. 1118, 1136 (2014) (discussing how cities crossing the line into insolvency are often marked with higher crime rates, low housing stock, blight, and unemployment).

163. *See Ex US Navy Base Has Become a Ghost Town*, TELEGRAPH (June 23, 2014, 11:08 AM), <http://www.telegraph.co.uk/news/worldnews/centralamericaandthecaribbean/puertorico/10919499/Ex-US-navy-base-has-become-a-ghost-town.html>; Andy Uhler, *Ponce, Puerto Rico: An Abandoned City*, MARKETPLACE (Apr. 12, 2016, 4:50 AM), <http://www.marketplace.org/2016/04/12/world/stranded-puerto-rico-debt/puerto-rico>.

164. Mario Mercado Diaz, *"This Town is Dead": The Long Decline of Arecibo, Puerto Rico*, COUNTERPUNCH (Aug. 18, 2015), <http://www.counterpunch.org/2015/08/18/this-town-is-dead-the-long-decline-of-arecibo-puerto-rico/>.

165. *See, e.g.*, WORKING GRP. FOR THE FISCAL AND ECON. RECOVERY OF PUERTO RICO, PUERTO RICO FISCAL AND ECONOMIC GROWTH PLAN (Sept. 9, 2015), <http://www.gdb-pur.com/documents/PuertoRicoFiscalandEconomicGrowthPlan9.9.15.pdf>; Charles Gasparino, *Wall Street's Disastrous 'Fix' for Puerto Rico*, N.Y. POST (July 13, 2015, 8:37 PM), <http://nypost.com/2015/07/13/wall-streets-disastrous-fix-for-puerto-rico/>.

166. *See, e.g.*, Preston Cooper, *The Federal Minimum Wage Is Killing Puerto Rico's Economy*, E21 (July 5, 2015), <http://economics21.org/html/federal-minimum-wage-killing-puerto-ricos-economy-1387.html>.

roots in progressive property theory because they strike at the heart of human flourishing—the notion that one should have the chance “to become fully developed persons in a particular social context” and that property law has a significant role to play in that endeavor.<sup>167</sup>

Last but certainly not least, environmental concerns are also embraced by the progressive account of property. The debt crisis and the accompanying austerity measures could not come at a worse time, as Puerto Rico has been recently hit with a number of natural disasters.<sup>168</sup> Droughts have plagued the island, with the U.S. Department of Agriculture declaring more than a quarter of the island a disaster area in July and again in August 2015.<sup>169</sup> Due to the drying up of the island’s reservoirs, the country declared a state of emergency and began a program of strict water rationing.<sup>170</sup> Thousands upon thousands of people on the island were only accorded access to tap water every third day, with the government further limiting the water supply to only two days a week during the height of the crisis.<sup>171</sup> Families across the island were forced to cook, bathe, and live on a limited number of gallons of water a week.<sup>172</sup> Businesses, particularly restaurants, suffered major losses.<sup>173</sup> The water rationing affected schools as well, disrupting classes and daily meals.<sup>174</sup>

While the two may seem unconnected, the debt crisis and the water crisis are deeply intertwined. The government, under fiscal panic for a number of years, has delayed spending money on capital improvements to water infrastructure like its reservoirs, aqueducts, and distribution systems.<sup>175</sup> Jose Molinelli-Freytes, a faculty member at the University of Puerto Rico specializing in environmental science, stated that, among other factors, the water crisis on the island is caused by “Puerto Rico’s aging and crumbling

167. Freyfogle, *supra* note 125, at 430 (citing Bennett & Mostert, *supra* note 125, at 6).

168. Alice Miranda Ollstein, *Water Rationing in Puerto Rico Hits the Poor, Leaves Resorts Untouched*, THINKPROGRESS (Aug. 10, 2015), <https://thinkprogress.org/water-rationing-in-puerto-rico-hits-the-poor-leaves-resorts-untouched-f81835288192#.wzx9e0kr6>.

169. *See id.*

170. *See id.*

171. *See id.*; *see also* Heather Janssen, *Puerto Rico Residents Face Water Rationing That Lasts up to 48 Hours Amid Historic Drought*, ACCUWEATHER (Aug. 15, 2015, 4:10 PM), <http://www.accuweather.com/en/weather-news/puerto-rico-drought-el-nino-tourism-local-water-restrictions/51647356>.

172. *See Ollstein, supra* note 168.

173. Chris Bury, *How Puerto Rico Is Coping with the Worst Drought in Decades*, PBS NEWSHOUR (Dec. 29, 2015, 6:30 PM), <http://www.pbs.org/newshour/bb/how-puerto-rico-is-coping-with-the-worst-drought-in-decades/>.

174. Ollstein, *supra* note 168.

175. *Id.*

water system.”<sup>176</sup> He stated that the “dams need maintenance” and the “reservoirs have too much silt and sediment.”<sup>177</sup> Professor Molinelli-Freytes further noted that the system’s “old water pipes routinely spring[] leaks” and cause “more than half of the water [to be lost] due to aging infrastructure and leaking.”<sup>178</sup> Unfortunately, the cash-strapped PRASA, with its \$4 billion in bonded debt, is hardly in any condition to undertake the improvements that are so desperately needed.<sup>179</sup> These environmental issues and issues related to access to food and agricultural resources—environmental morality—are also an integral part of social property claims.<sup>180</sup>

The stories above paint a clear picture of an island in crisis—and more broadly, the troubles of jurisdictions facing financial insolvency. Crushing debt is taking a human toll on the people of Puerto Rico, and so the Commonwealth’s advocates rightly advance arguments related to human dignity as part of their larger push for congressional relief.<sup>181</sup> But property comprises “social interests, such as environmental stewardship, civic responsibility, and aggregate wealth.”<sup>182</sup> It encapsulates “human interaction to ensure that people relate to each other with respect and dignity.”<sup>183</sup> These conceptions of property are part and parcel of the human dignity concerns of the Puerto Ricans.<sup>184</sup> Indeed, property rights are embodied in the human dignity claims of all persons living in

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176. *Id.*

177. *See id.*

178. *Id.*; see also Eric Holthaus, *Be Thankful, California. At Least You’re Not Puerto Rico*, SLATEST (June 22, 2015, 12:48 PM), [http://www.slate.com/blogs/the\\_slatest/2015/06/22/drought\\_in\\_puerto\\_rico\\_it\\_s\\_much\\_worse\\_than\\_california.html](http://www.slate.com/blogs/the_slatest/2015/06/22/drought_in_puerto_rico_it_s_much_worse_than_california.html) (“John Morales, a Miami-based meteorologist who provides weather forecasting services for the Caribbean, said Puerto Rico’s government could actually be underestimating the seriousness of the problem. . . . The capacity of the reservoirs has been severely compromised by sedimentation and lack of maintenance, Morales told me. What’s worse, he said the island’s ‘crumbling infrastructure’ is producing ‘huge losses’ of water from innumerable leaks.”).

179. Michelle Kaske, *Which Puerto Rico Bond Defaults Next? 42% Yields Provide a Clue*, BLOOMBERG (Dec. 28, 2015, 12:01 AM), <http://www.bloomberg.com/news/articles/2015-12-28/which-puerto-rico-bond-defaults-next-42-yields-provide-a-clue> (“[PRASA]: \$4.1 billion. The utility, called [PRASA], supplies most of the island’s water. The debt is repaid from water rates charged to customers. The water agency owes \$86.5 million of interest in January and \$135.1 million of principal and interest in July. Bonds maturing in 2042 last traded at a yield of 9.1 percent.”).

180. *See* Freyfogle, *supra* note 125, at 448.

181. *See* Alexander et al., *supra* note 123, at 743.

182. *Id.*

183. *See id.*

184. *See id.* (“Values promoted by property include life and human flourishing, the protection of physical security, the ability to acquire knowledge and make choices, and the freedom to live one’s life on one’s own terms. They also include wealth, happiness, and other aspects of individual and social well-being.”).

jurisdictions on the verge of bankruptcy. It is through this notion of social property, finding its grounding in the progressive account, that one sees the interconnecting nature of property rights and human concerns, such as public health, environmental well-being, and economic prosperity. This vision of property moves beyond merely the traditional rights and duties of a thing and its owner. Rather, it presses property law further, resulting in a paradigm that exemplifies the larger constellation of human needs and societal aspirations. It is through this vision of property law that the Puerto Ricans and others living in insolvent jurisdictions may claim a right in property—social property.

## 2. *Property Rights and the People Behind the Investments*

Much of the narrative around the bondholders' claims has been equally one-sided and overly simplistic. Supporters of the island frame the debt issue as one of "hedge fund exploitation."<sup>185</sup> They highlight recent instances, such as the July 2015 report issued by Centennial Group International, where certain bondholders suggested cuts to taxes for the wealthy, cuts to educational expenses, eliminating or lowering the minimum wage, and privatizing public assets.<sup>186</sup> Political advertisements declare that "people are literally dying as a result of Wall Street's greed."<sup>187</sup> Reports tell of hedge funds using their political leverage to get paid, even before Puerto Rico pays its hospitals and doctors.<sup>188</sup> Advocates for the island paint a picture of investment funds that identify vulnerable economies—like Detroit, Greece, and Argentina—and squeeze them for everything they are worth.<sup>189</sup> These hedge funds, often called "vulture funds," are known for purchasing the sovereign debt of distressed economies at deep discounts with the aim of reaping significant profits later.<sup>190</sup> They also have the power to influence, stall, or even paralyze debt-restructuring negotiations.<sup>191</sup>

185. The Undercurrent, *Hedge Funds Are Deepening Humanitarian Crisis in Puerto Rico*, YOUTUBE (Nov. 20, 2015), <https://www.youtube.com/watch?v=UuSdRop2ZnM>.

186. Jose Fajgenbaum et al., CENTENNIAL GRP. INT'L, FOR PUERTO RICO, THERE IS A BETTER WAY 5 (July 2015), <http://www.centennial-group.com/downloads/For%20Puerto%20Rico%20There%20is%20a%20Better%20Way.pdf>.

187. Brave New Films, *Greed 101: Hedge Funds Bringing Poverty and Suffering to Places Like Puerto Rico*, YOUTUBE (June 10, 2016), <https://www.youtube.com/watch?v=VrOcXTOPvQA>.

188. *See id.*

189. *See id.*

190. Jonathan C. Lippert, *Vulture Funds: The Reason Why Congolese Debt May Force a Revision of the Foreign Sovereign Immunities Debt Act*, 21 N.Y. INT'L L. REV. 1, 2 (2008); Tim R Samples, *Rogue Trends in Sovereign Debt: Argentina, Vulture Funds, and Pari Passu Under New York Law*, 35 NW. J. INT'L L. & BUS. 49, 52 (2014).

191. Christopher C. Wheeler & Amir Attaran, *Declawing the Vulture Funds: Rehabilitation of a Comity Defense in Sovereign Debt Litigation*, 39 STAN. J.

Indeed, they have tried to do as much in the case of Puerto Rico, with many of them serving as plaintiffs in litigation related to the island's recent attempts to restructure its debt without Congress.<sup>192</sup> Under such facts, it is indeed hard to imagine how such parties could possibly raise even the slightest claim to human dignity when it comes to the island paying its debt.

The truth, however, is much more complicated. Those holding jurisdictional debt in an insolvency crisis are always viewed as the "bad guys" even though their story is often more nuanced than that.<sup>193</sup> While there are groups of investors that have specifically targeted Puerto Rico due to its vulnerable financial state, they make up a minority of the total number of bondholders.<sup>194</sup> In all, so-called vulture funds hold about 35% of the total amount of the island's public debt—enough to cause problems when it comes to an amicable workout with the island's government, but not a majority.<sup>195</sup>

Putting aside Wall Street hedge funds and their vulture money managers, a tremendous portion of the American public—ranging from schoolteachers to retirees to blue collar workers—stand to

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INT'L L. 253, 254 (2003); Ed Morales, *How Hedge Funds and Vulture Funds Have Exploited Puerto Rico's Debt Crisis*, NATION (July 21, 2015), <https://www.thenation.com/article/how-hedge-and-vulture-funds-have-exploited-puerto-ricos-debt-crisis/>.

192. See Lawrence Delevingne, *Hedge Fund Sues Puerto Rico over New Bond Law*, CNBC (July 22, 2014, 3:32 PM), <http://www.cnbc.com/2014/07/22/hedge-fund-sues-puerto-rico-over-new-bond-law.html> (discussing claims by one of the major hedge funds—Blue Mountain Fund); Daniel Siegal, *Creditors Sue for Puerto Rico Gov't Bank Withdrawal Freeze*, LAW360 (Apr. 4, 2016, 11:43 PM), <http://www.law360.com/articles/780173/creditors-sue-for-puerto-rico-gov-t-bank-withdrawal-freeze> (discussing claims by the Brigade Capital Management, Claren Road Asset Management, and Fore Research & Management LP funds).

193. Danica Coto, *Puerto Rico Bondholders Devastated, but See Hope in US Plan*, WASH. POST (Aug. 1, 2016), [https://www.washingtonpost.com/world/the-americas/puerto-rico-bondholders-devastated-but-see-hope-in-us-plan/2016/08/01/975546f0-57fb-11e6-8b48-0cb344221131\\_story.html](https://www.washingtonpost.com/world/the-americas/puerto-rico-bondholders-devastated-but-see-hope-in-us-plan/2016/08/01/975546f0-57fb-11e6-8b48-0cb344221131_story.html).

194. Laura J. Keller, *Puerto Rico's \$72 Billion Mess Reunites Lehman Foes*, BLOOMBERG NEWS (June 2, 2015, 12:00 AM), <http://www.bloomberg.com/news/articles/2015-06-02/puerto-rico-s-72-billion-distress-mess-reunites-lehman-era-foes> ("Hedge funds now hold as much as 30 percent of the obligations of Puerto Rico and its agencies, Barclays Plc municipal-debt strategist Mikhail Foux estimates.").

195. Ellie Ismailidou, *3 Things to Know About Puerto Rico's Debt Moratorium*, MARKETWATCH (Apr. 15, 2016, 4:38 PM), <http://www.marketwatch.com/story/3-things-to-know-about-puerto-ricos-debt-moratorium-2016-04-13> ("Around 36% to 37% are owned by hedge funds."); Marc Joffe, *Opinion, Why Hedge Funds May Not Get a Windfall from Puerto Rico*, FISCAL TIMES (Apr. 26, 2016), <http://www.thefiscaltimes.com/Columns/2016/04/26/Why-Hedge-Funds-May-Not-Get-Windfall-Puerto-Rico> ("In all, hedge funds own an estimated 36 percent of Puerto Rico's outstanding bond obligations.").

suffer from Puerto Rico failing to pay its debt.<sup>196</sup> The reason for this is, as with many public debt disputes, there are a number of mutual funds that are significantly exposed to Puerto Rican debt, “with a couple in excess of 40 percent.”<sup>197</sup> As one fund analyst noted, “half of U.S. open-ended municipal-bond funds hold some exposure to the debt of [Puerto Rico] . . . [F]unds collectively own more than \$11.4 billion of the island[']s debt or just over 15% of its outstanding issuance.”<sup>198</sup> Morningstar reports that “more than 300 mutual funds, or 52% of all muni bond funds” have some level of exposure to Puerto Rican debt.<sup>199</sup> The reason for the prevalence of Puerto Rican debt in the American economy is simple. As noted above, Puerto Rican bonds are triple-tax-exempt—interest payments are not taxed at any level in any jurisdiction.<sup>200</sup> Because of this, many funds that hold money for retirees, for seniors saving for retirement, for working Americans, and for those saving for college have invested heavily in Puerto Rican municipal debt.<sup>201</sup> That means there are a lot of people in the United States who are holding the island’s debt, whether they know it or not.

A number of these at-risk funds are familiar names for most American households. Oppenheimer Fund and Franklin Templeton Investments—both well known and widely utilized mutual funds for many<sup>202</sup>—are two of the largest single holders of the Commonwealth’s public debt.<sup>203</sup> These funds are now understandably concerned about the position of their investments—investments made on behalf of millions of everyday working Americans. For instance, in the case of Oppenheimer, “[t]en of its 20 muni funds have at least a 15 percent stake in junk-rated Puerto Rico. Nine of those rank in the bottom 10 percent of their peer

196. Coto, *supra* note 193.

197. Jeff Cox, *Fund Managers Have Been Running from Puerto Rico Debt*, CNBC (May 10, 2016, 2:46 PM), <http://www.cnbc.com/2016/05/10/fund-managers-have-been-running-from-puerto-rico-debt.html>.

198. Adam Shapiro, *Puerto Rico Default Risk Could Impact Average Americans*, FOX BUSINESS (July 31, 2015), <http://www.foxbusiness.com/markets/2015/07/31/puerto-rico-default-impacts-average-americans.html>.

199. Jeff Benjamin, *Puerto Rico’s Uncertain Future Leaves Muni Bond Fund Investors in Limbo*, INV. NEWS (Aug. 3, 2015, 12:40 PM), <http://www.investmentnews.com/article/20150803/FREE/150809989/puerto-ricos-uncertain-future-leaves-muni-bond-fund-investors-in>.

200. Greenberg & Ekins, *supra* note 62.

201. *Id.*

202. Mutual funds are used for investment purposes and are comprised of pools of money collected by a large number of investors to invest in various securities, such as stocks and bonds, at the direction of fund managers. See generally JOHN A. HASLEM, MUTUAL FUNDS (2010) (detailing the operation and purposes of mutual funds). The major advantage of a mutual fund is that it allows very small investors to participate in sophisticated equity and debt markets with the help of investment professionals. *Id.*

203. See Shapiro, *supra* note 198.

group.”<sup>204</sup> The Franklin Double Tax-Free Income Fund, a fund of Franklin Templeton Investments, fared even worse—declining 2.1 percent annually—due to the fact that half of all of its assets are in Puerto Rican bonds.<sup>205</sup>

The rest of the bonds (the largest portion—those not owned by hedge funds or mutual funds) are owned by actual individual investors.<sup>206</sup> This includes everyday Americans, both on the mainland and in Puerto Rico. The significance of this cannot be understated, particularly for Puerto Ricans who themselves have invested in the island’s public debt. As one commentator stated of people on the island: “We have a lot of people who are seniors and they depend on the returns from those bonds to live on a month-to-month basis.”<sup>207</sup>

While it might be easy for the supporters of debt relief for Puerto Rico to vilify the faceless bondholders, there are many middle-income, hardworking Americans who form a part of that group. This is often the case in any public debt crisis.<sup>208</sup> Those who invest in public debt are not merely the lords of Wall Street. They come from Main Street as well. And, indeed, they have claims, not merely based in property law, but in human concerns as well.<sup>209</sup>

To make this point even clearer, it is helpful to compare the Puerto Rican debt crisis to the narrative that dominated (and continues to dominate) the 2008 financial crisis. Indeed, we can learn a lot about what is at stake for public debt bondholders—like those who invested in Puerto Rico’s debt in anticipation of retirement or savings—from remembering the victims of the 2008 crisis. Similar to the case of the Puerto Rican creditors and other creditors of insolvent jurisdictions,<sup>210</sup> banks and other institutions

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204. Brian Chappatta, *Puerto Rico Teaches Oppenheimer Funds Perils of Hunting for Yield*, BLOOMBERG (Dec. 14, 2015, 12:00 AM), <http://www.bloomberg.com/news/articles/2015-12-14/puerto-rico-teaches-oppenheimerfunds-perils-of-hunting-for-yield>.

205. *See id.*

206. Heather Long, *Who Owns Puerto Rico’s Debt?*, CNN MONEY (Aug. 6, 2015, 7:06 PM), <http://money.cnn.com/2015/07/01/investing/puerto-rico-bond-holders/>.

207. *Id.*

208. Laurence Siegel, *Can We Recover from the Public Debt Crisis? Of Course We Can*, ADVISOR PERSP. (June 9, 2015), <http://www.advisorperspectives.com/articles/2015/06/09/can-we-recover-from-the-public-debt-crisis-of-course-we-can>.

209. Marlene Y. Satter, *Puerto Rico Debt Woes Could Hit Retirees, Retirement Plans Hard*, BENEFITSPRO (Apr. 22, 2016), <http://www.benefitspro.com/2016/04/22/puerto-rico-debt-woes-could-hit-retirees-retiremen>.

210. Mike Boehm, *Detroit’s Creditors Want Entire Art Museum Collection to Be Fair Game*, L.A. TIMES (May 30, 2014, 3:06 PM), <http://www.latimes.com/entertainment/arts/culture/la-et-cm-detroit-institute-of-arts-city-bankruptcy-20140530-story.html>; Yvonne R. Walker, *Wall Street About to Win in Stockton*

involved in the financial crisis were certainly viewed as the chief villains of the crash.<sup>211</sup> Their financial freewheeling and often fraudulent practices played an enormous and central role in bringing about the crisis.<sup>212</sup> Nevertheless, even in that instance there were human stories behind the cold glass of Wall Street. Many of the institutions that purchased, or even engaged in the creation of these toxic financial products, did so with other people's money—often the money of hard-working Americans saving for their children's education or for their own retirement.<sup>213</sup>

Everyday Americans took a major hit as a result of the U.S. financial crisis, much like what today faces the Commonwealth's bondholders and the creditors of many governments in distress like Jefferson County, Stockton, and Detroit.<sup>214</sup> By the end of 2008, the S&P 500 lost 37% of its value for the year.<sup>215</sup> In that same period, retirement accounts lost over \$1.6 trillion dollars (18.3% of their total value).<sup>216</sup> That number ballooned to \$1 trillion a mere fifteen months after the crash.<sup>217</sup> The Employee Benefit Research Institute

at *Expense of Middle Class*, SACRAMENTO BEE (Oct. 19, 2014, 5:00 PM), <http://www.sacbee.com/opinion/op-ed/soapbox/article2963119.html>. See generally PAUL BLUSTEIN, *AND THE MONEY KEPT ROLLING IN (AND OUT)* (2005) (explaining the role played by major financial institutions in Argentina's 2001 financial crash).

211. NAT'L COMM'N ON THE CAUSES OF THE FIN. & ECON. CRISIS IN THE U.S., *THE FINANCIAL CRISIS INQUIRY REPORT*, at xvii (Jan. 2011), <https://www.gpo.gov/fdsys/pkg/GPO-FCIC/pdf/GPO-FCIC.pdf>.

212. KATHLEEN C. ENGEL & PATRICIA A. MCCOY, *SUBPRIME VIRUS* 30–31 (2011); SUZANNE MCGEE, *CHASING GOLDMAN SACHS* 4–7 (2010).

213. JOHN KAY, *OTHER PEOPLE'S MONEY* 163–64 (2015); see also Robert Lenzner, *The Dangerous Opacity of Modern Banking*, ATLANTIC (Oct. 21, 2015), <http://www.theatlantic.com/business/archive/2015/10/wall-street-other-peoples-money/411694/>.

214. Robin Respaut, *Holdout Creditor in Stockton Bankruptcy Denied Higher Claim*, REUTERS (Dec. 10, 2014, 6:44 PM), <http://www.reuters.com/article/usa-stockton-franklin-idUSL1N0TU28X20141210> (discussing the claims of Franklin Templeton Investments—a fund used by a large number of American seniors and retirees); Mike Wilkinson, *Here's a Short List of the 8 Detroit Creditors Who Will Win and Lose the Most*, MICH. PUB. RADIO (Mar. 27, 2014), <http://michiganradio.org/post/heres-short-list-8-detroit-creditors-who-will-win-and-lose-most#stream/0> (discussing cuts to retirement benefits for certain pension creditors).

215. JACK VANDERHEI, *THE IMPACT OF THE RECENT FINANCIAL CRISIS ON 401(K) ACCOUNT BALANCES* 1 (2009), [https://www.ebri.org/pdf/briefspdf/EBRI\\_IB\\_2-2009\\_Crisis-Impct.pdf](https://www.ebri.org/pdf/briefspdf/EBRI_IB_2-2009_Crisis-Impct.pdf).

216. Richard W. Johnson et al., *How Is the Economic Turmoil Affecting Older Americans?*, URBAN INST. (Oct. 7, 2008), <http://www.urban.org/research/publication/how-economic-turmoil-affecting-older-americans>.

217. *The Effects of Recent Turmoil in Financial Markets on Retirement Security Before the H. Comm. on Educ. & Labor*, 110th Cong. 2 (2008), [https://www.cbo.gov/sites/default/files/110th-congress-2007-2008/reports/10-07-retirementsecurity\\_testimony\\_0.pdf](https://www.cbo.gov/sites/default/files/110th-congress-2007-2008/reports/10-07-retirementsecurity_testimony_0.pdf) (statement of Peter R. Orszag, Director, Cong. Budget Office).

reported that 401(k) investment accounts lost anywhere from 7% to nearly 12% in the first nine months of 2008.<sup>218</sup> Naturally, this hit baby boomers the hardest.<sup>219</sup> It can take years for a nest egg to recover from such violent dips in the market, and the baby boomer group unfortunately did not have that time to wait.<sup>220</sup> Many seniors were forced to go back to work as the incomes that they once depended on shrank.<sup>221</sup> Unfortunately, many discovered that finding work was difficult, as workforce needs and skills requirements had changed—with competition for jobs becoming evermore intense.<sup>222</sup>

The same sort of human concerns apply to holders of public debt. They too are everyday Americans working hard to save for the future. Massive defaults or being forced to take deep cuts on their investments can have a significant negative effect on their financial futures. Because of this, their story is not one based merely in claims to “payment” and “property rights” in their investments, but rather in the real consequences of how sometimes only a slight change in investment performance can lead to serious financial distress. Oftentimes it is those least able to cope with such a life change that a financial crisis hits the hardest, and the investors in Puerto Rico and other public debt creditors like them are little different.

It is through this lens that we should see the claims of the creditors—as ones that also encompass human dignity concerns. While it is true that there are some investors who approach investments in sovereign debt from a purely speculative nature, there are many who trust money managers to make wise investments to help them plan for the future. It is these individuals, faceless and nameless in a public debt crisis and never at the bargaining table, who truly represent the human aspects of the creditors’ claims.

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218. *The Impact of the Financial Crisis on Workers’ Retirement Security Before the H. Comm. on Educ. & Labor*, 110th Cong. 4 (2008), <https://www.ebri.org/pdf/publications/testimony/t156.pdf> (statement of Jack VanDerhei, Research Dir., Emp. Benefit Research Inst.).

219. Craig Guillot, *How the Financial Crisis Impacts Your Retirement*, CNBC (Nov. 19, 2008, 1:54 PM), <http://www.cnbc.com/id/27806491>.

220. *See id.*

221. Emily Brandon, *Why More Americans Are Working Past Age 65*, U.S. NEWS (Feb. 11, 2013, 9:40 AM), <http://money.usnews.com/money/retirement/articles/2013/02/11/why-more-americans-are-working-past-age-65>.

222. Katy Read, *The Real Story About Retirement: Millions of Baby Boomers Face Financial Crisis*, STARTRIBUNE (Oct. 21, 2015, 9:56 AM), <http://www.startribune.com/the-real-story-about-retirement-millions-of-baby-boomers-face-financial-crisis/334718191/>.

## II. WHY PUBLIC BANKRUPTCY LAW NEEDS A PROPERTY THEORY REFORMATION

Having established that neither side of the Puerto Rican debt crisis has an exclusive claim to property rights or human dignity concerns, this Part argues that, rather than being merely interwoven from a theoretical standpoint, these two concepts should be more deeply connected from a doctrinal perspective as well. In order to do this, I describe and classify the Commonwealth's debt and then analyze how that debt would be treated under existing Takings Clause and Bankruptcy Clause doctrine. In conducting this analysis, I show that case law has failed to properly conceptualize property law and human values as interlocking principles, evidenced by the way courts have given disparate and rigid treatment to different forms of debt, without appreciating the larger societal concerns at play in debt recomposition and whether a more fluid process would achieve better ends. I then argue, using the Puerto Rican debt crisis as a backdrop, that courts should reform their thinking on property law in insolvency proceedings by embracing a more progressive view of property rights—a view that sees and interprets property rights through the lens of public welfare.<sup>223</sup> Bankruptcy law needs a property theory transformation.

### A. Bankruptcy Law and the Classification of Debt

Before thinking about what a property-theory makeover would look like, we need to know how property law is currently viewed in the bankruptcy context. The Takings Clause provides that private property cannot be taken by the government without a public purpose and without the provision of just compensation.<sup>224</sup> Drilling down into Takings Clause law, we know that the purpose of the clause itself is to prevent the government, as Justice Black noted in *Armstrong v. United States*,<sup>225</sup> from “forcing some people alone to bear public burdens [that], in all fairness and justice, should be borne by the public as a whole.”<sup>226</sup> The most recognizable form of takings is that involving the government actually appropriating or otherwise physically invading the property of private persons, such as when the state takes property for use as a road or for public utilities.<sup>227</sup> It is often said that this form of taking is “as old as the

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223. See Joseph William Singer, *The Reliance Interest in Property*, 40 STAN. L. REV. 611, 687 (1988) (discussing how relationships and reliance inform property rights).

224. U.S. CONST. amend. V.

225. 364 U.S. 40 (1960).

226. *Id.* at 49.

227. See *Rindge Co. v. Los Angeles Cty.*, 262 U.S. 700, 710 (1923); *Mt. Vernon-Woodberry Cotton Duck Co. v. Alabama Interstate Power Co.*, 240 U.S. 30, 32–33 (1916).

Republic.”<sup>228</sup> However, the property claims inherent in the case of public debt recomposition do not concern this type of taking. Rather, these claims hinge on a takings theory of a “more recent vintage”—the so-called “regulatory taking”<sup>229</sup> that was first formally established in 1922 by the Supreme Court in *Pennsylvania Coal Co. v. Mahon*.<sup>230</sup>

Regulatory takings are those whereby the government engages in an action that, although not directly dispossessing the owner of his property, restricts that owner’s ability to use the property to such a degree that the action is tantamount to a physical dispossession.<sup>231</sup> Although the form is different between physical and regulatory takings, the practical effect is nearly the same.<sup>232</sup> Examples of governmental actions that can bring about a regulatory taking include “[z]oning laws, environmental protection laws, historical preservation laws, and public health and safety laws.”<sup>233</sup> The recomposition or modification of public debt (or any debt), therefore, raises regulatory takings concerns.<sup>234</sup> Puerto Rico’s case is no different.

There are three sequential steps to any type of takings claim.<sup>235</sup> First, a constitutionally protected property interest must be identified.<sup>236</sup> While there may indeed be an interest in property at play, not all such interests are afforded constitutional protection.<sup>237</sup> Second, it must be determined that this interest was taken by the government for a public purpose.<sup>238</sup> Lastly, it must be determined if just compensation was afforded to the owner as a result of the deprivation.<sup>239</sup>

228. *Tahoe-Sierra Pres. Council, Inc. v. Tahoe Reg’l Planning Agency*, 535 U.S. 302, 322 (2002).

229. *Id.*

230. 260 U.S. 393 (1922).

231. Gregory M. Stein, *Regulatory Takings and Ripeness in the Federal Courts*, 48 VAND. L. REV. 1, 7–8 (1995).

232. *See id.*

233. *See id.* at 8–9.

234. Peter L. Cockrell, Comment, *Subprime Solutions to the Housing Crisis: Constitutional Problems with the Helping Families Save Their Homes Act of 2009*, 17 GEO. MASON L. REV. 1149, 1194 (2010); *see* Thomas E. Plank, *Bankruptcy and Federalism*, 71 FORDHAM L. REV. 1063, 1090 n.106 (2002); Tabb, *supra* note 24, at 801–02.

235. *See Mehta v. Surles*, 905 F.2d 595, 598 (2d Cir. 1990).

236. *Fletcher v. City of New Haven*, No. 3:11-cv-00708-AWT, 2012 WL 1032967, at \*2 (D. Conn. Mar. 27, 2012).

237. *See id.*; *see also* Rachal D. Cox, Note, *Placing a Value on Community: U.S. v. 0.073 Acres of Land and the Compensability of the Right to Collect Assessments*, 42 S.U. L. REV. 361, 380 (2015) (describing where federal courts have declined to give “property status” to restrictive covenants).

238. *See Amen v. City of Dearborn*, 718 F.2d 789, 789 (6th Cir. 1983).

239. *Carson Harbor Village, Ltd. v. City of Carson*, No. CV-90-3428-LEW, 1991 WL 634911, at \*8 n.1 (C.D. Cal. Apr. 9, 1991).

One part of regulatory takings claims is the notion of “investment-backed expectations.”<sup>240</sup> In 1978, the U.S. Supreme Court formally introduced this concept in connection with regulatory takings disputes in the case of *Penn Central Transportation Co. v. City of New York*.<sup>241</sup> In that case, the owners of Grand Central Terminal, through a lessee, planned to conduct an expansion that included a high-rise office building to be constructed above the station.<sup>242</sup> However, the building had previously been designated as a historical landmark, which resulted in the city’s planning commission rejecting the new project.<sup>243</sup> The owners and lessee then sued, claiming that the designation of the building as a landmark amounted to a taking of their property interests in the station.<sup>244</sup> Deciding the case on appeal, Justice Brennan introduced a new test to be used in regulatory takings litigation. This three-part test requires a court to evaluate (1) “the character of the governmental action,” (2) “[t]he economic impact of the regulation,” and (3) the extent to which the action interferes with “reasonable investment-backed expectations.”<sup>245</sup> The Court noted that the plaintiffs’ “primary expectation concerning the use of the parcel” as a rail station was not interfered with as a result of the landmark designation.<sup>246</sup> Thus, no taking of property had occurred.<sup>247</sup>

Now, admittedly, the jurisprudence regarding regulatory takings has been decried by many as being hopelessly confusing. Professor Steven Eagle notes that the doctrine “has become a compilation of moving parts that are neither individually coherent nor collectively compatible.”<sup>248</sup> This Article does not attempt to replicate or do better what countless property scholars have attempted in the past—to articulate a coherent and fair regulatory

240. Daniel R. Mandelker, *Investment-Backed Expectations in Taking Law*, 27 URB. LAW. 215, 215 (1995).

241. 438 U.S. 104 (1978).

242. *Id.* at 116.

243. *Id.* at 115–17.

244. *Id.* at 119.

245. *Id.* at 124; see Julie Patterson Forrester, *Bankruptcy Takings*, 51 FLA. L. REV. 851, 865 (1999).

246. See *Penn Central Transp. Co.*, 438 U.S. at 136.

247. *Id.* at 138. In the later case of *Lucas v. South Carolina Coastal Council*, the Supreme Court further illuminated the takings analysis by stating that in certain situations there is no need to evaluate the *Penn Central* factors, but rather a taking exists per se. See *Lucas v. S.C. Coastal Council*, 438 U.S. 1003, 1015 (1978). This consists of situations where there is a “physical ‘invasion’ of . . . property” as well as those where government regulation denies a property owner “all economically beneficial or productive use” of his property. *Id.* The only limitation to the latter exception is when the denial is based on “background principles of the State’s law of property and nuisance already placed upon land ownership.” *Id.* at 1029.

248. Steven J. Eagle, *The Four-Factor Penn Central Regulatory Takings Test*, 118 PENN. ST. L. REV. 601, 602 (2014).

takings doctrine.<sup>249</sup> Rather, this Article seeks to explain how the regulatory takings doctrine can and should reconcile social interests and property rights in the context of distressed public debt—or more specifically, in contract rights that create debt like the government-issued bonds of Puerto Rico, its municipalities, and its public corporations.

In order to do that, it is necessary to have some doctrinal knowledge (to complement the theoretical understanding) about how debt and property are actually connected. Since 1923, the Supreme Court has held that rights in a contract (such as a bondholder's right in debt) constitute property rights that are protected by the Fifth Amendment's Takings Clause.<sup>250</sup> Indeed, for quite some time courts held categorically that contracts create property rights.<sup>251</sup> The court in *Omnia Commercial Co. v. United States* held, "[t]he contract in question was property within the meaning of the Fifth Amendment."<sup>252</sup> Again, in *Lynch v. United States*<sup>253</sup> the Court held that "[v]alid contracts are property, whether the obligor be a private individual, a municipality, a State or the United States."<sup>254</sup> Thus, rights "arising out of a contract with [the United States] are protected by the Fifth Amendment."<sup>255</sup>

### B. Property Rights Only for the Secured

This absolutist treatment of contract rights, however, is not so absolute in the context of bankruptcy. In other words, sometimes contracts rights are property and sometimes they are not—all depending on whether we are inside or outside of bankruptcy proceedings. The U.S. Constitution grants Congress the power to enact uniform bankruptcy laws, and the operation of this constitutional provision interacts with the Takings Clause in a way

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249. See generally J. Peter Byrne, *Property and Environment: Thoughts on an Evolving Relationship*, 28 HARV. J.L. & PUB. POL'Y 679 (2005); Marc R. Poirier, *The Virtue of Vagueness in Takings Doctrine*, 24 CARDOZO L. REV. 93 (2002); Shelley Ross Saxon, *The Fluid Nature of Property Rights in Water*, 21 DUKE ENVTL. L. & POL'Y F. 49 (2010) (creating a fair regulatory takings doctrine).

250. *U.S. Tr. Co. v. New Jersey*, 431 U.S. 1, 33 (1977) (Brennan, J., dissenting) (recognizing the "property rights embodied in a contract"); *City of El Paso v. Simmons*, 379 U.S. 497, 534 (1965) (Black, J., dissenting) ("[T]he Contract Clause protects the value of the property right in contracts . . ."); *Lynch v. United States*, 292 U.S. 571, 579 (1934) ("Valid contracts are property, whether the obligor be a private individual, a municipality, a State, or the United States."); *Omnia Commercial Co., Inc. v. United States*, 261 U.S. 502, 508 (1923) (representing the first case holding that rights in a contract form property rights).

251. *Omnia Commercial Co.*, 261 U.S. at 508.

252. *Id.*

253. 292 U.S. 571 (1934).

254. *Id.* at 579.

255. *Id.*

that curtails an overly categorical view of contracts as property.<sup>256</sup> In fact, within the context of bankruptcy, contract rights related to debt obligations (i.e., property rights) can be modified without per se constituting a taking.<sup>257</sup> This rule is not necessarily unexpected. The very purpose of bankruptcy law, as Justice Story states, is “for the benefit and relief of creditors and their debtors, in cases, in which the latter are unable, or unwilling to pay their debts.”<sup>258</sup> That necessarily means that if the creditor is to be relieved of paying his debts at all or in full, a diminution of the creditor’s right (property right) in the debt must occur. In order to accommodate this goal, Takings Clause considerations would have to yield to those of the Bankruptcy Clause. Therefore, creditors could not arrest nor frustrate the goal of giving the distressed debtor a fresh start by claiming an unconstitutional taking of property.

But, the Supreme Court, to the chagrin of others,<sup>259</sup> has not adopted this logic. In the seminal case of *Louisville Joint Stock Land Bank v. Radford*,<sup>260</sup> the Court made clear that the Takings Clause does indeed limit the bankruptcy powers of Congress, but in a very inflexible and rather discriminating way.<sup>261</sup> In other words, only some kinds of debt (read: property), when modified in bankruptcy, bring about Takings Clause consequences. The distinction then turns not on whether there is a property right in the debt generally, but rather whether the debt at issue is *secured*. Specifically, Fifth Amendment considerations in the bankruptcy context change depending on whether the creditor’s claim is secured by a lien on other property.<sup>262</sup> Section 506 of the Bankruptcy Code indicates that a secured claim is one that is “secured by a lien on property in which the [bankruptcy] estate has an interest.”<sup>263</sup> In other words, the property right in the debt must itself be secured by property before Takings Clause considerations can be raised. The mere debt itself (as property) is not enough. Therefore, in bankruptcy, credit card debt (which is unsecured) would not be property, but mortgage loan debt (secured by a lien on real estate)

256. U.S. CONST. art. 1, § 8, cl. 4.

257. See Tabb, *supra* note 24, at 800–01.

258. JOSEPH STORY, 2 COMMENTARIES ON THE CONSTITUTION OF THE UNITED STATES 60 n.2 (3d ed. 1858).

259. See, e.g., Rogers, *supra* note 47, at 984.

260. 295 U.S. 555 (1935).

261. See *id.* at 568, 589.

262. See generally Thomas E. Plank, *The Constitutional Limits of Bankruptcy*, 63 TENN. L. REV. 487 (1996) (arguing that Congress can only regulate the relationship between debtor and creditors, and thus bankruptcy law should neither benefit nor harm third parties at the expense or benefit of debtors and creditors).

263. 11 U.S.C. § 506 (2012).

would be property.<sup>264</sup> Outside of bankruptcy, courts would equally treat both sets of debt as property.<sup>265</sup>

With that understanding, the next question becomes how that system actually treats secured versus unsecured creditors (and subsequently, how the various Puerto Rican creditors—like all public debt creditors—should be classified and treated). The important distinction between being secured and unsecured, as discussed briefly above, is this: Congress *can* modify contract rights that are not secured by collateral without causing Takings Clause problems (despite the fact that the contracts themselves, even without collateral, are a form of property according to the Supreme Court), but Congress *cannot* modify the creditors' rights in the collateral itself without raising Takings Clause issues. The nature of property rights in debt was best stated (and most frequently

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264. It is important to recognize why a discussion of property rights in the context of bankruptcy is relevant for Puerto Rico, as it would be for other American jurisdictions, like Detroit and Stockton, utilizing Chapter 9 of the Bankruptcy Code. PROMESA purports to be animated by Congress's authority under the territories power—the exclusive ability of Congress to make all “needful rules and regulation for the territories.” S. 2328, 114 Cong. § 101(b)(2) (2016). Nevertheless, since this legislation appears to involve the composition of public debts, it seems more than likely that the Supreme Court, when ultimately called upon to answer the question, would hold that Congress is also acting pursuant to its powers under the Bankruptcy Clause. Although Congress is creating something completely new—rather than tying into the existing federal bankruptcy regime—the Court has in prior cases stated that the Bankruptcy Clause's power reaches beyond what might technically be considered “bankruptcy” and rather extends to laws that affect insolvency more broadly. See *Sturges v. Crowninshield*, 17 U.S. (4 Wheat.) 122, 194–95 (1819); see also *Cont'l Ill. Nat'l Bank & Tr. Co. v. Chi., Rock Island & Pac. Ry. Co.*, 294 U.S. 648, 671 (1935); *Hanover Nat'l Bank v. Moyses*, 186 U.S. 181, 186 (1902). Justice Story similarly described the bankruptcy power as being that which “is a law making provisions for cases of persons failing to pay their debts.” STORY, *supra* note 258, at 60 n.2. The passage of PROMESA could be considered similar to Congress's passage of the District of Columbia Financial Responsibility and Management Assistance Act of 1995 (which was enacted under its constitutional power “[t]o exercise exclusive Legislation in all Cases whatsoever, over” D.C.) that sought to address a financial crisis in the federal capitol in the mid-1990s. U.S. CONST. art 1, § 8, cl. 17. But that legislation too was related to the handling of public debts, and municipal bankruptcy law loomed large in the background. See Gillette, *Dictatorships for Democracy*, *supra* note 82, at 1396 n.123. Therefore, it seems logical that disputes among creditors broadly holding property rights in their debt under *Omnia Commercial Co.* may nevertheless find their rights interpreted under the bankruptcy / Fifth Amendment constitutional framework discussed. *Supra* Subpart II.A. Thus, analyzing the property claims of the bondholders under the bankruptcy regime is appropriate here as it would be under more traditional public insolvency proceedings.

265. See Russ Cope, *What's More Dangerous: Credit Card or Mortgage Debt?*, COPE LAW OFFICES, LLC BLOG (Nov. 24, 2014), <http://www.daytonbankruptcyfirm.com/whats-dangerous-credit-card-mortgage-debt/>.

repeated in later cases) by Justice Douglas in *Wright v. Union Central*<sup>266</sup> when he proclaimed that a creditor's property claim in his debt is limited only "to the extent of the value of the [collateral]. . . . There is no constitutional claim of the creditors to more than that."<sup>267</sup> This, of course, leaves unsecured creditors in a most unfortunate position. Despite having a property interest in the debt broadly, within the context of the Bankruptcy Clause the "property" right is not really property at all.

### C. *Whose Puerto Rican Debt is Secured?*

With this background, the final inquiry is then how do we classify the debt of public creditors? Indeed, we can easily say that if a loan is secured by collateral, it is a secured debt (like a home loan or a car loan).<sup>268</sup> If debt is not secured (like a student loan or a credit card loan), then it is unsecured.<sup>269</sup> But public debts are different. Creditors holding public debt do not have mortgages on public land to secure the right to get paid. Indeed, most state constitutions prohibit such transactions.<sup>270</sup> So, in which category do Puerto Rico's creditors fall? In other words, how would takings law treat the Puerto Rican creditors in a congressional insolvency framework, and does such treatment adequately resolve the property and human dignity concerns inherent in the claims of all parties? Before answering that question, it is helpful (if not necessary) to understand the composition of Puerto Rico's \$72 billion debt, because the status of each debt category has the potential to affect how courts might handle constitutional concerns raised in connection with a restructuring.<sup>271</sup> In other words, who is secured, and who is unsecured in Puerto Rico?

Not all public bondholders are created equal. Public bonds can be broken up into general obligation bonds and revenue bonds. Using Puerto Rico as a lens, the Commonwealth has around \$12.6 billion in general obligation debt outstanding (with hundreds of millions of dollars due in interest).<sup>272</sup> Payment of these is guaranteed, like all general obligation bonds, by the full faith and credit and taxing power of the island's government.<sup>273</sup> Importantly, there is no direct stream of tax or fee revenue that guarantees

266. 311 U.S. 273 (1940).

267. *Id.* at 278.

268. *Secured Debt*, BLACK'S LAW DICTIONARY (10th ed. 2014).

269. *Unsecured Debt*, BLACK'S LAW DICTIONARY (10th ed. 2014).

270. See ROBERT S. AMDURSKY ET AL., MUNICIPAL DEBT FINANCE LAW 330–32, 654–56 (2d ed. 2013).

271. For a discussion of the Fifth Amendment implications for secured versus unsecured creditors, see *infra* Subpart III.B.2.

272. Kristi Culpepper, *What Does Puerto Rico's Debt Crisis Mean for Bondholders?*, MEDIUM (Sept. 25, 2015), <https://medium.com/@munilass/what-does-puerto-rico-s-debt-crisis-mean-for-bondholders-6dfb0e893f80#.wr650keen>.

273. *Id.*

repayment. Rather it is from the general finances and taxing power of Puerto Rico that payment is to be accomplished.<sup>274</sup> Broadly speaking, general obligation bonds are considered unsecured because they lack the backing of a concrete interest of the issuer.<sup>275</sup> Conversely, revenue bonds are generally considered to be secured debt because they are backed by the pledge of a particular asset of the issuer (usually a stream of revenue derived from a fee or other charge).<sup>276</sup>

However, such a simple explanation hides the truth. The way in which the island's government has made general obligation bonds attractive is to enshrine a provision into the Commonwealth's constitution stating that "[i]n case the available revenues including surplus for any fiscal year are insufficient to meet the appropriations made for that year, interest on the public debt and amortization thereof shall first be paid."<sup>277</sup> As some commentators have noted, the government has given conflicting signals—sometimes stating that it will not give general obligation bondholders special treatment and at other times declaring that it will prioritize their claims in accordance with the constitution.<sup>278</sup> Not long ago the island's legislature repealed a provision that had long benefited general obligation bond holders—a requirement that a certain amount of money be set aside each year to meet general obligation bond debt.<sup>279</sup> Puerto Rico, like many governments, often overlays its general obligation debt with special statutory or constitutional provisions that would suggest that the debt is actually accorded some form of special treatment.

Another major portion of the debt pie comes in the form of bonds issued by the Puerto Rico Sales Tax Financing Corporation (called, in Spanish, "COFINA").<sup>280</sup> This is a public corporation that was created in 2006 to help refinance various debt obligations of the island—in other words, its sole purpose is to be a refinancing vehicle.<sup>281</sup> The corporation receives half of the island's sales tax

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274. See *id.*

275. See, e.g., *In re Sanitary & Improvement Dist. No. 7*, 98 B.R. 970, 973–74 (Bankr. D. Neb. 1989).

276. Michael L. Hall & George D. Gaskin, III, *Municipal Bonds in Chapter 9: A Primer*, AM. BANKR. INST. J., Jul/Aug 2011, at 38, 39.

277. See P.R. CONST. art. VI, § 8; see also *id.* at Art. VI, § 2 ("The Secretary of the Treasury may be required to apply the available revenues including surplus to the payment of interest on the public debt and the amortization thereof in any case provided for by Section 8 of this Article VI at the suit of any holder of bonds or notes issued in evidence thereof.").

278. See Culpepper, *supra* note at 272.

279. See *id.*

280. See Kaske & Braun, *supra* note 95.

281. Act. No. 291, H.R. 3163 § 2 (2006), <http://www.oslpr.org/download/en/2006/A-0291-2006.pdf>.

revenues that are collected by the central government.<sup>282</sup> COFINA's debt comprises about \$15.2 billion of the total.<sup>283</sup>

In no particular order of priority, next comes the Puerto Rico Electric Power Authority, the island's main electrical power supplier, which has \$9 billion in debt.<sup>284</sup> The revenues used to pay this debt are derived from customer charges.<sup>285</sup> This is followed by the \$4.7 billion in debt owed by the PRHTA, the revenues of which come from gas taxes.<sup>286</sup>

The PRASA (the island's main water supplier), the GDB (which loans money to the central government and many local governments of the Commonwealth), and the Public Buildings Authority (which manages the leasing and operation of public buildings) owe at least \$4 billion each.<sup>287</sup> The Infrastructure Financing Authority (whose revenues come from rum taxes) owes \$1.85 billion, and the Public Finance Corporation (which is a bank of last resort that helps cover government deficits from time to time, the monies of which are solely derived from legislative appropriation) owes \$1.1 billion.<sup>288</sup>

Last but not least, an issue that is not unknown to local governments and states in the United States,<sup>289</sup> \$2.9 billion is owed on Puerto Rico's pension obligation bonds.<sup>290</sup> These bonds are issued by the island to meet the ongoing pension obligations of the various retirement systems (both for the central and municipal

282. See Culpepper, *supra* note 272.

283. *Id.*

284. Mary Williams Walsh, *How Free Electricity Helped Dig \$9 Billion Hole in Puerto Rico*, N.Y. TIMES, DEALBOOK (Feb. 1, 2016), <http://www.nytimes.com/2016/02/02/business-dealbook/puerto-rico-power-authoritys-debt-is-rooted-in-free-electricity.html>.

285. Michelle Kaske, *Puerto Rico's Electric Utility Extends Pact to Pay Bonds*, BLOOMBERG (June 30, 2016, 1:59 PM), <http://www.bloomberg.com/news/articles/2016-06-30/puerto-rico-power-utility-avoids-july-1-default-with-bond-deal>.

286. Culpepper, *supra* note 272.

287. Michelle Kaske & Sowjana Sivaloganathan, *Puerto Rico Faced Record Default: A Look at the Bonds Due*, BLOOMBERG (June 30, 2016, 12:39 PM), <http://www.bloomberg.com/news/articles/2016-06-30/puerto-rico-faces-record-default-a-look-at-the-2-billion-due>.

288. *Id.*

289. See Marilyn Cohen, *Investors, Just Say No to Illinois, NJ and PR Muni Bonds*, FORBES (Dec. 11, 2014, 9:33 AM), <http://www.forbes.com/sites/investor/2014/12/11/investors-just-say-no-to-illinois-nj-and-pr-muni-bonds/#7bb454ac3223>; Steven Malanga, *The Muni-Bond Debt Bomb*, CITY J. (2010), <http://www.city-journal.org/html/muni-bond-debt-bomb-13298.html> ("States and cities have also used muni debt to play dangerous games in the stock and bond markets. A particularly potent weapon in the politicians' debt arsenal is the so-called pension-obligation bond, the municipal equivalent of borrowing money on your credit card to make contributions to your IRA.")

290. Kaske & Sivaloganathan, *supra* note 287.

governments).<sup>291</sup> There is a specific revenue stream matched to each debt issuance, but there is always the chance that the legislature or some other political authority will decrease the revenue stream, redirect it, or eliminate it altogether. Indeed, that is the political process at work, and that uncertainty makes the notion of creditor reliance quite uneasy.

So how do the concepts of secured versus unsecured debt comport with the concepts of revenue bonds and general obligation bonds? The question of labeling is not so easily answered when it comes to public debt. For instance, depending on the constitutional or statutory provision governing an issuer's general obligation bonds, some general obligation bonds can be considered secured.<sup>292</sup> One bankruptcy court handling a 1980s Chapter 9 proceeding in Nebraska noted that although the general obligation bonds of the debtor municipality were technically unsecured, payment to holders of those bonds should be given priority.<sup>293</sup> This was because a state statute required that the local government impose a special tax if there were ever a lack of funds necessary to pay the general obligation bonds—thereby making them much more akin to secured debt.<sup>294</sup> Similarly, sometimes revenue bonds, nominally backed by a specific revenue source, can nonetheless be deemed unsecured.<sup>295</sup>

As one can imagine from the public finance and bankruptcy discussion above, the distinction between being secured and unsecured in the Puerto Rican crisis will end up mattering a great deal because of the many different types of bondholders who will be fighting for a limited amount of Commonwealth revenues. This is not just a Puerto Rico problem—this is always the case in public debt disputes. As noted above, the Fifth Amendment requires that secured claimants receive the sale value of their pledged collateral, but unsecured claimants do not have Fifth Amendment protections.<sup>296</sup> To that point, some analysts believe that one of the big creditor fights in the Puerto Rican crisis will be between the

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291. *Id.* To round out the total, the island's Convention Center District Authority owes \$397.7 million to its bondholders, and the agency derives its revenues from hotel-occupancy taxes. *Id.*

292. *See, e.g., In re Orange Cty.*, 189 B.R. 499, 503 (Bankr. D. Cal. 1995).

293. *See Hall & Gaskin, supra* note 276, at 39.

294. *See id.*

295. *See, e.g., KPMG, LLP, MARQUETTE UNIVERSITY: FINANCIAL STATEMENTS JUNE 30, 2014 AND 2013*, at 29 (Sept. 5, 2014), <http://www.marquette.edu/financeoffice/documents/FinancialAuditFY14.pdf> ("All of the revenue bonds are unsecured."); *Moody's Revises Valparaiso University's (IN) Outlook to Negative; Affirms A2*, MOODY'S INV'RS SERV. (Jan. 15, 2016), [https://www.moodys.com/research/Moodys-revises-Valparaiso-Universitys-IN-outlook-to-negative-affirms-A2-PR\\_903029856](https://www.moodys.com/research/Moodys-revises-Valparaiso-Universitys-IN-outlook-to-negative-affirms-A2-PR_903029856) ("The university's educational facilities revenue bonds are unsecured general obligations of the university and have no debt service reserve fund.").

296. *See Patrick A. Murphy, Restraint and Reimbursement: The Secured Creditor and Arrangement Proceedings*, 30 BUS. LAW. 15, 23 (1974).

general obligation bondholders and the holders of COFINA bonds.<sup>297</sup> Although it would seem that the constitution protects the former to the prejudice of the latter, there are a number of legal structures in place that attempt to insulate the sales tax revenues that go to the COFINA bondholders from being rerouted.<sup>298</sup> For instance, although the constitution states that the general obligation bondholders are to be paid from “available resources” of the Commonwealth, the sales tax revenues directed to COFINA debt are put into a lock box, and the statute setting up this accounting structure has a nonimpairment provision.<sup>299</sup> Most trained lawyers would say that the constitutional provision trumps the statute’s firewall, but that all depends on what constitutes “available resources.”<sup>300</sup>

Noted bond analyst Kristi Culpepper points out that back in 2007 the island’s legislature passed a law stating that the sales tax revenues dedicated to COFINA “shall not constitute available resources of the Commonwealth of Puerto Rico for any purpose, including for the purpose of Section 8 of Article VI of the Constitution.”<sup>301</sup> This appears to create a carve out for COFINA funds in order to escape the constitutional rights of general obligation bondholders. Whether courts will allow this legislative act to prejudice the constitutional rights of general obligation bond creditors seems, at first blush, unlikely—but the ultimate result remains unclear.

Which bondholders are secured (for instance, whether the holders of the Commonwealth’s general obligation bonds are secured creditors by virtue of constitutional revenue preferences) and which are not (such as whether the revenue bondholders are actually unsecured because of the constitutional preference for general obligation bonds), as well as how the Fifth Amendment will play into creditors’ abilities to combat efforts to overly reduce their rights to payment, is a matter that remains unsettled. That means there will likely be more than just a little fighting among the island’s creditors once a debt restructuring process is commenced. Ultimately it would be the judge overseeing the insolvency proceeding who would make the determination, but, as Professor Melissa Jacoby has pointed out recently, even in the context of the now-famous 2013 bankruptcy of Detroit, the court often did not

297. See, e.g., Culpepper, *supra* note 272.

298. *Id.*

299. *Id.*; P.R. CONST. art. VI, § 2.

300. See generally Jacob Scott, *Codified Cannons and the Common Law of Interpretation*, 98 GEO. L.J. 341 (2010) (discussing how legislatures generally do not mean for their statutes to violate constitutional provisions).

301. Culpepper, *supra* note 272 (quoting Leg. P.R. 56, 15th Leg., 5th Sess. (P.R. 2007)).

handle the secured versus unsecured question directly.<sup>302</sup> Rather, the judge strongly encouraged the parties to settle the matter in negotiations led by a different federal judge—a process that was conducted largely behind closed doors.<sup>303</sup> This is because the question over secured status is so difficult in the context of public debt. It is easy enough to tell who is secured when you are dealing with private parties—with a business or in consumer bankruptcy. But when legislatures and local governments send mixed signals as to the status of debt on the front end, it is difficult (if not impossible) to make a determination on the back end—at least not in a way that avoids making distinctions that appear superficial.

### III. A PROGRESSIVE PROPERTY APPROACH TO PUBLIC DEBT RECOMPOSITION

Our current constitutional understanding of property rights in the context of bankruptcy is deeply flawed. It draws artificial and inconsistent lines between what is property and what is not, creates needless disputes between parties to debt recomposition proceedings, and obstructs reasoned governmental policy decisions about the resolution of public debt emergencies. In other words, bankruptcy law needs a property theory redo.

The bridge to getting from our current doctrinal way of thinking to a more optimal paradigm is the progressive property movement.<sup>304</sup> Through a more holistic and pluralistic view of property rights, the law can come to better reflect the laudable policy goals inherent in public insolvency proceedings. The Supreme Court's current contemplation of property rights in the context of the Takings Clause and the Bankruptcy Clause does not adequately reflect the interlocking nature of human values and private entitlements. But it should, and it can—and progressive property theory can provide the way.

#### A. *Rejecting the Secured-Unsecured Property Paradigm*

The first thing that needs to be done in order to reform property theory in bankruptcy is to dispense with the bifurcation of property rights.<sup>305</sup> This Article is not the first to find fault with the Supreme Court's view that only secured claims should be given Takings Clause protections in bankruptcy. Professor Charles Tabb has most recently written extensively about the history of the Bankruptcy

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302. Melissa B. Jacoby, *Federalism Form and Function in the Detroit Bankruptcy*, 33 YALE J. REG. 55, 99–100 (2016).

303. *See id.*

304. *See, e.g.,* Tabb, *supra* note 24, at 805–09 (arguing that the current approach distinguishing secured and unsecured debt needs to change).

305. *See* Rogers, *supra* note 47, at 988–89; Tabb, *supra* note 24, at 804.

Clause and its development in the context of takings claims.<sup>306</sup> He also disputes the logic and correctness of the rule that only secured claims are property within the meaning of the Takings Clause. He succinctly crystallizes the Court's faulty rule by saying that "the expectations deserving takings protection are simply weaker in a contract setting than when there is a lien."<sup>307</sup> In doing so, Tabb rejects the notion that secured claims should be treated any differently than unsecured claims when it comes to the modification of debt in bankruptcy.<sup>308</sup> He notes the troublesome and internally inconsistent approach that the Court appears to adopt in this area—focusing particularly on business bankruptcies.<sup>309</sup>

To use Tabb's words, "The only honest way to harmonize the two is to reason that contract rights are a sort of 'property-light' in the specific context of bankruptcy for takings purposes, as compared to lien rights as property."<sup>310</sup> The constitutional line is drawn, according to Tabb, on the principle that "a secured creditor has a right to have its claim paid . . . claiming thereby a tangible 'stick' in the bundle of property rights" that constitutes "a protectable property interest" as opposed to unsecured creditors who "only have a general claim against the debtor."<sup>311</sup> He notes that this is the case despite the fact, as noted above, that the Supreme Court has already stated on countless occasions that contracts by themselves (without secured collateral) constitute property rights within the meaning of the Constitution.<sup>312</sup>

In thinking about public bankruptcies and in looking through the lens of Puerto Rico's debt crisis, I too reject the notion that property rights should be bifurcated in this fashion and also that they should be so narrowly construed. Why should the holders of general obligation bonds have a superior position vis-à-vis other bonds holders? For that matter, in the case of Puerto Rico, what is the overarching policy reason for COFINA bondholders to have superior rights to payment from the general obligation bondholders? One possible reason is investor risk. Bonds are priced to take into

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306. Tabb, *supra* note 24, at 800 ("[N]o one doubts that there is no Fifth Amendment takings problem when a contract-as-property claim is discharged pursuant to a bankruptcy law. Assuming that such is a correct conclusion, and I submit that it is, that then means that a supporter of the position that the Takings Clause limits what can be done to secured creditors in bankruptcy must identify a constitutionally distinguishable basis for treating the two types of 'property' differently. I do not believe that case can be made.")

307. *Id.* at 799.

308. *See id.* at 800.

309. *See id.* at 801.

310. *Id.* at 802.

311. *Id.* at 805.

312. *See id.* at 802.

account risk.<sup>313</sup> That is, a general obligation bond is priced differently than a revenue bond for the very reason that the revenue bondholder is taking a different risk than the general obligation bondholder.<sup>314</sup> From that perspective, it might be optimal to allow this kind of bifurcation in order both to efficiently allocate risks and to maximize governments' access to capital markets. In short, it may make financial sense to allow governments to have creditors with different priorities.

While this argument sounds compelling, the devil is in the details. As noted in the example of Puerto Rico, the government typically does not make clear (perhaps purposefully so) which debt has priority.<sup>315</sup> The investor's risk expectations end up being fought about in court as parties try to ascertain what the legislature really meant when they seemed to simultaneously grant special treatment to different categories of debt.<sup>316</sup> With such twisted constitutional provisions and confusing statutory roadmaps, how can one really say with certainty that one group is secured by the pledge of specific revenues while the other is not? For that matter, if the island is in serious financial distress and the point of the bankruptcy power is to give the debtor a fresh start while still doing justice to the property rights of the bondholders, why does a purported form of collateral (and a phantom one at that) even matter? Bondholders can never truly be secured like a mortgagee or the holder of a Uniform Commercial Code Article 9 interest.<sup>317</sup> Rather, here they can only make legal arguments as to how obscurely drafted statutes, constitutional provisions, and bond resolutions should be interpreted—whether they give preference to one creditor over

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313. See *In re Healthsouth Corp. Sec. Litig.*, 261 F.R.D. 616, 632 (N.D. Ala. 2009) (“Bonds generally are rated as investment-grade bonds or speculative-grade (‘junk’) bonds. . . . [T]he degree of risk finds its way into the market price of the bonds.”).

314. See 64 AM. JUR. 2D *Public Securities and Obligations* § 13 (2d ed. 2011) (noting that general obligation bonds are secured by the taxing powers of the issuer, whereas revenue bonds are generally only payable with the revenue funds derived from the improvement the bond funded).

315. See Philip R. Wood, *The Bankruptcy Ladder of Priorities*, 14 BUS. L. INT’L 209, 212 (2013) (noting that “there are conventions as to priorities and sometimes priority is seized by one set of creditors over others,” but generally, there is “no explicit ladder of priorities mandated by the law” when a sovereign debtor defaults).

316. See, e.g., *NML Capital, Ltd. v. Republic of Argentina*, 699 F.3d 246, 251 (2d Cir. 2012) (litigating Argentina’s failure to pay holders of defaulted Fiscal Agency Agreement bonds after converting a portion of those bonds into Exchange Bonds, which subsequently received priority in payment).

317. See Horacio T. Liendo III, *Sovereign Debt Litigation Problems in the United States: A Proposed Solution*, 9 OR. REV. INT’L L. 107, 109–11 (2007) (noting that private sector creditors can generally pursue a debtor’s assets, but that is not “a viable solution” to a creditor holding defaulted sovereign bonds because typically, restructuring of sovereign debt occurs without an enforcement mechanism to ensure payments to bondholders).

another.<sup>318</sup> At the very least, such dealings introduce one more thing for bondholders, the oversight board, and the island to fight about, and at worst, it deprives the bankruptcy process from having the latitude and flexibility it needs to justly mediate between the property and dignity claims of the creditors and those of the people of Puerto Rico.

Important to Tabb's normative point, however, is the principle that the Bankruptcy Clause alone empowers and limits Congress's ability to deal with property interests inside the arena of bankruptcy.<sup>319</sup> In other words, "[t]he Takings Clause . . . simply should not be treated as an independent limitation on the operation of congressional power under the Bankruptcy Clause."<sup>320</sup> While I wholeheartedly agree with Tabb as to his critique of why the Court's treatment of secured versus unsecured debt has led to negative results (and would do so here in the case of Puerto Rico and in other public bankruptcies), this Article does not ultimately take the view that it is necessary for us to separate congressional power into the discreet silos of the Bankruptcy Clause or the Takings Clause. Indeed, it is not necessary or desirable to segregate these two sources of power into such restrictive categories at all. Instead, the Bankruptcy Clause and the Takings Clause can be harmonized with one another in a way that breaks down the problematic barrier that Tabb identifies.

In order to achieve this, the Court must expand its normatively confined view of the Takings Clause to better incorporate the notion that property rights and the policy objectives inherent in bankruptcy can be reconciled without necessarily causing one constitutional provision to yield to the other. The debt crisis in Puerto Rico highlights the importance of such a constitutional reconciliation. On both sides of the crisis, there are property rights and humanitarian concerns—concerns that are implicit in the policy of bankruptcy, which is geared toward giving debtors a “fresh start.”<sup>321</sup> The progressive property movement provides the needle and thread to tie these concepts together.

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318. See generally SERGIO M. MARXUACH, CTR. FOR A NEW ECON., THE ENDGAME: AN ANALYSIS OF PUERTO RICO'S DEBT STRUCTURE AND ARGUMENTS IN FAVOR OF ENACTING A COMPREHENSIVE DEBT RESTRUCTURING MECHANISM FOR PUERTO RICO (2016), <http://bit.ly/2aBM7X3> (explaining, for example, that the language of the Constitution of Puerto Rico regarding the payment of general obligation bonds says “available resources” in Spanish but “available revenues” in English, that it is unclear if any issued bonds beside general obligation bonds have nonacceleration or *pari passu* covenants, and so forth).

319. See Tabb, *supra* note 24, at 772 (“Properly understood, the only limitation on the scope of congressional power under the Bankruptcy Clause inheres in the Bankruptcy Clause itself.”).

320. *Id.* at 809.

321. Nathalie D. Martin, *Noneconomic Interests in Bankruptcy: Standing on the Outside Looking in*, 59 OHIO ST. L.J. 429, 437 n.29 (1998).

*B. Proposing a Constitutional Framework for Progressive Debt-Property*

Human dignity shapes the scope and allocation of property rights. Indeed, the Constitution itself does this by both requiring the payment of debts (by virtue of the Contracts Clause<sup>322</sup> and the Takings Clause)<sup>323</sup> and by allowing bankruptcy (through the Bankruptcy Clause)<sup>324</sup> to discharge those debts so as to allow people to receive a fresh start and move on. The very conflict at play in the Puerto Rican debt crisis and all public debt crises is built into the U.S. Constitution, and that constitutional dialogue suggests that these things are not “in tension” but are, in fact, wed and need to be interpreted together. Progressive property scholarship provides the tool with which this realization can be properly theorized and implemented.

As noted above, a progressive view of property law calls for an understanding that rights in property are relational and cross wide fields to reach parties that might seem distant to the owner but are, in fact, quite closely bound to the thing itself.<sup>325</sup> Certainly, while pro-owner doctrines should not be completely jettisoned, there is, as Professor Eric Freyfogle notes, a need to “interject[] further elements into the discussion.”<sup>326</sup> Specifically, the notion is that “private ownership entails responsibilities in addition to rights.”<sup>327</sup> Strong individual-based rights in property remain in place, but they are tempered and qualified with “attendant duties” such as those due to “neighbours, to communities as such, and to opposing parties in property transactions.”<sup>328</sup>

Thus, the rights of public bondholders have strong owner-centric aspects to them, but those rights are touched and shaped by duties that are owed to the people in whose name such debt was issued.<sup>329</sup> It is not unjust, nor does it injure property rights, for

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322. U.S. CONST. art. I, § 10, cl. 1.

323. U.S. CONST. amend. V.

324. U.S. Const. art. I, § 8, cl. 4.

325. See Freyfogle, *supra* note 125, at 430–31 (discussing three progressive views on property rights: (1) arguing that property rights should evolve to encourage “human flourishing,” bolstering social relationships and personal development; (2) arguing property rights should reflect the “social order” laid out in the South African Constitution, built on “widespread, equitable” access to resources; and (3) arguing that theories of property rights should abandon the “rights paradigm” in order to discuss private ownership absent the historical presumption favoring existing owners. Freyfogle concludes the article by proposing that any modern intellectual analysis of property rights consider the social responsibilities of ownership).

326. *Id.* at 452.

327. *Id.*

328. *Id.*

329. See *id.* (asserting that owners of property—who retain “strong individual rights”—would have to qualify their rights through their duties owed to “opposing parties” in litigation).

bondholders to see their rights to payment modified or even diminished, because in so acquiring such debt the bondholders also acquired “inchoate responsibilities.”<sup>330</sup> Baked into creditor rights is the larger societal duty for which the law necessarily must mediate in times of public distress. That mediation comes in the form of bankruptcy proceedings—like the PROMESA process unfolding for Puerto Rico or the Chapter 9 process used for Stockton, Detroit, and others<sup>331</sup>—by providing a vehicle for humanitarian concerns and property rights to live alongside one another: a goal that the Constitution should facilitate. Rather than treating debts categorically, bankruptcy courts should be empowered, under the direction of Congress, to judge and assess the different interests at stake in a public debt crisis and craft a solution that meets the needs of that particular situation. In breaking down the disparate treatment between secured and unsecured holders of debt, investors might *all* receive some allocation of property rights in the form of payment. In turn, the Puerto Ricans will not be relieved of their obligation to pay their debts, but rather will be given the opportunity to do so on terms that respect human values and allow the people to enjoy basic goods and services—to maintain their dignity.

It might seem as though these theoretical arguments are too aspirational and too divorced from the current state of the law to ever persuade the Court to exercise greater flexibility when dealing with creditors and debtors in public financial distress. But in fact, as the following shows, the notion of inchoate responsibilities is not actually new to the Supreme Court’s interpretation of the Takings Clause.<sup>332</sup> Unfortunately, this progressive approach to property rights in debt claims has never been allowed to reach its fullest potential. Consider the Supreme Court’s 1970 decision in the so-called *New Haven Inclusion Cases*<sup>333</sup>—a decision that truly strikes at the heart of how property rights in public debt and larger societal concerns interact and are ultimately resolved under the Constitution.<sup>334</sup> In that series of cases, the New York, New Haven & Hartford Railroad (“New Haven”) was in the middle of a

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330. *Id.*

331. *Bankrupt Cities, Municipalities List and Map*, GOVERNING.COM, <http://www.governing.com/gov-data/municipal-cities-counties-bankruptcies-and-defaults.html> (last visited Nov. 27, 2016) (listing all U.S. municipal bankruptcies since January 1, 2010—fifty-one filings in all).

332. *See New Haven Inclusion Cases*, 399 U.S. 392, 408–09 (1970) (detailing the obligations incurred by Penn Central in its acquisition of the New Haven railroad lines).

333. *Id.*

334. *See id.* at 493–95 (holding there was no constitutional unfairness in conditioning the permission of the merger between Penn Central and New Haven on the complete inclusion and continued operation of the New Haven rail line).

tremendous financial crisis and was undergoing a merger with Penn Central Railroad in order to save it from utter ruin.<sup>335</sup> As part of the merger, Penn Central would acquire all of the assets of New Haven, in exchange for giving \$125,000,000 (later raised to \$162,700,000) to the defunct railroad company's bondholders.<sup>336</sup> The holders of New Haven's bonded indebtedness, however, argued that this price was insufficient, and in forcing them to accept an insufficient price, the government was depriving them of a property right protected by the Fifth Amendment.<sup>337</sup>

In addressing this claim, the Court stated that while "security holders 'cannot be called upon to sacrifice their property so that a depression-proof railroad system might be created'" they nevertheless "invested their capital in a public utility that does owe an obligation to the public."<sup>338</sup> Further elaborating on this point, the Court stated that "by their entry into a railroad enterprise, [they] assumed the risk that in any depression or any reorganization the interests of the public would be considered as well as theirs."<sup>339</sup> The Court then quoted from its earlier decision in the *Penn-Central Merger Cases*,<sup>340</sup> where it stated that "[i]t is a fundamental aspect of our free enterprise economy that private persons assume the risks attached to their investments, and the N[ew] H[aven] creditors can expect no less because the N[ew] H[aven]'s properties are devoted to a public use."<sup>341</sup> Lastly, the Court commented on the constitutional property interests of the bondholders when confronted with competing interests (particularly those of a more national character):

While the rights of the bondholders are entitled to respect, they do not command Procrustean measures. They certainly do not dictate that rail operations vital to the Nation be jettisoned despite the availability of a feasible alternative. The public interest is not merely a pawn to be sacrificed for the strategic purposes or protection of a class of security holders. . . .<sup>342</sup>

Here, one sees a balancing of interests between private property entitlements and rival public policy concerns. This is the same intertwining of interests at play in the Puerto Rico situation and

335. *Id.* at 408.

336. *Id.* at 412-13, 415.

337. *Id.* at 489-90.

338. *Id.* at 491-92 (quoting *Reconstruction Fin. Corp. v. Denver & R.G.W.R. Co.*, 328 U.S. 495, 535-36 (1946)).

339. *Id.* at 492 (alteration in original) (quoting *Reconstruction Fin. Corp.*, 328 U.S. at 535-36).

340. *Penn-Cent. Merger & N & W Inclusion Cases*, 389 U.S. 486 (1968).

341. *Id.* at 510 (quoting *Penn. R.R. Co.—Merger—N.Y. Cent. R.R. Co.*, 331 I.C.C. 643, 704 (1967)).

342. *Id.* at 510-11.

fiscal crises like it. The property rights and human dignity concerns advanced by the bondholders and the Puerto Rican government should inform the Court to apply the same reasoning as to how the Court resolved the *New Haven Inclusion Cases*. In applying the Court's interpretation in that case to the property rights and human dignity concerns of the bondholders and the Puerto Rican people, it follows that while "security holders 'cannot be called upon to sacrifice their property so that'" a completely fiscally healthy and debt-free Puerto Rico can be achieved, they nevertheless "invested their capital in a public [body] that does owe an obligation to the public."<sup>343</sup> By virtue of having done so, these creditors "assumed the risk that in any depression or any reorganization the interests of the public would be considered as well as theirs."<sup>344</sup>

To be sure, the law must respect and afford protection to the property rights of bondholders in public debt so that commercial transactions will not be irreparably harmed. That is what regulatory-takings law contemplates. But the respect due to these rights does "not command Procrustean measures."<sup>345</sup> They most certainly do not, and for the sake of a fair and just system of laws cannot, dictate the operations, services, and functions of governments like that of Puerto Rico, which in all right belongs to the people.<sup>346</sup> Joseph Singer makes this point eloquently when he states that that takings doctrine "does not immunize owners from the rule of law or democratic governance."<sup>347</sup> The humanity and dignity of both the people of the Commonwealth and the bondholders inform and guide the law's view of property rights—they are not separate or adversarial. Although a forced restructuring or even moratorium may indeed result in an economic impact on the bondholders, as Singer so correctly notes, what matters is "the *type* of impact at issue, not the *size* of the impact."<sup>348</sup> In other words, the nature and the character of the impact is what should drive the Court's takings analysis. Echoing Justice Stewart's words: "The public interest is not merely a pawn to be sacrificed for the strategic purposes or protection of a class of security holders."<sup>349</sup>

Additional evidence of jurisprudential leanings toward a more progressive view of property rights in the context of debt can be found in the concurrence to the Supreme Court's 1982 decision in

343. *New Haven Inclusion Cases*, 399 U.S. at 491–92 (1970).

344. *See id.* at 492 (quoting *Reconstruction Fin. Corp.*, 328 U.S. at 535–36).

345. *Id.* (quoting *Penn-Cent. Merger Cases*, 389 U.S. at 510–11).

346. *See* William Joseph Singer, *Property as the Law of Democracy*, 63 DUKE L.J. 1287, 1301 (2014).

347. William Joseph Singer, *Justifying Regulatory Takings*, OHIO N.U. L. REV. 601, 608 (2015).

348. *Id.* at 607.

349. *Penn-Cent. Merger Cases*, 389 U.S. at 511.

*United States v. Security Industrial Bank*.<sup>350</sup> In that case, various creditors loaned money to debtors in exchange for liens on various household goods and appliances, all done before the 1978 bankruptcy statute was enacted,<sup>351</sup> which allowed for these types of liens to be avoided.<sup>352</sup> Thereafter, the debtors sought bankruptcy protection and attempted to invoke the 1978 avoidance procedure.<sup>353</sup> The bankruptcy court refused to apply the 1978 avoidance provision retroactively so as to remove the liens from the household appliances of the debtors.<sup>354</sup> The debtors appealed, arguing that Congress explicitly intended for the 1978 statute to be applied retroactively.<sup>355</sup>

When the case reached the Supreme Court, the Court rejected retroactive application and thereby avoided addressing the ultimate constitutional issue of whether doing so would have constituted a taking.<sup>356</sup> Nevertheless, the concurrence, led by Justice Blackmun and joined by Justices Brennan and Marshall, indicated some approval for the progressive property movement's notion that "[p]roperty rights are based on law and defined and redefined over time . . . in an effort to promote the common good."<sup>357</sup> Justice Blackmun wrote that if retroactivity had applied, he still would not have found a compensable taking.<sup>358</sup> He based this on a multifaceted analysis—essentially judging the compensability of the impairment of the creditor's lien on a sliding scale, measured by how minimally invasive the application of the avoidance procedure would be on the creditor's rights against the relative fairness concerns as to the debtor.<sup>359</sup> Importantly, he put special emphasis on the "salutary" policy rationale behind the avoidance procedure: "to give the debtor a fresh start with a minimum for necessities."<sup>360</sup> As suggested by Freyfogle in the context of redefining property rights to meet the common good, the concurrence declared that Congress is within its power to "adjust priorities."<sup>361</sup>

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350. 459 U.S. 70, 83 (1982).

351. See 11 U.S.C. § 522(f)(2) (2012).

352. See *Penn-Cent. Merger Cases*, 389 U.S. at 74.

353. See *id.* at 74–77.

354. *Id.* at 71.

355. *Id.* at 72.

356. *Id.* at 81 ("An early version of the 1978 Act contained an explicit requirement that all its provisions 'shall apply in all cases or proceedings instituted after its effective date, regardless of the occurrence of any of the operative facts determining legal rights, duties or liabilities hereunder.' . . . Congress' elimination of an explicit command is some evidence that it did not intend to depart from the usual principle of construction [that statutes be given only prospective application].").

357. Freyfogle, *supra* note 125, at 453.

358. See *Sec. Indus. Bank*, 459 U.S. at 83–84.

359. *Id.* at 84.

360. *Id.*

361. *Id.*

Justice Blackmun's concurrence in *Security Industrial Bank* admittedly placed a special emphasis on the fact that the creditors held a lien (and were secured), but his arguments are nonetheless significant here.<sup>362</sup> Although it does not represent the majority's view, it correctly expresses how the Court should treat property rights and competing social interests in the context of bankruptcy. His rationale is particularly important because it reconciles the human dignity concerns and property claims of both parties in a way that respects both. His rationale also blends the human concerns and property claims so as not to force one to yield to the other, but rather for property to be cognizant of social considerations. The concurrence signals with approval the role that "salutary" policy concerns can play in the constitutional analysis.<sup>363</sup> In the context of Puerto Rico, the salutary effect of giving the Commonwealth a chance to reorganize its debts and still meet the basic human needs of its citizens is driven by a view of property rights that incorporates human values and their claims to social property. It is within this context that the Takings Clause and the policies that underpin the Bankruptcy Clause speak to one another.

Lastly, even more recent cases have hinted toward a broader view of property rights.<sup>364</sup> These cases do so by alluding to the fact that "[r]esponsibilities and virtues are taken into account when defining [property] rights, not tacked on later."<sup>365</sup>

In the wake of the 2008 financial crisis, the federal government took a number of measures in order to save many large financial institutions from disaster.<sup>366</sup> These institutions included Fannie Mae and Freddie Mac (the mortgage finance giants that shortly prior to the crash either guaranteed or outright owned 40% of all U.S. residential mortgage debt)<sup>367</sup> and AIG (a Wall Street financial institution that, in the run-up to the crash, entered into complex derivative contracts called credit default swaps with various parties that ended up costing the company trillions of dollars in liabilities that it could not hope to pay).<sup>368</sup>

362. *See id.* at 82–85.

363. *Id.* at 84.

364. *See, e.g.,* *Starr Int'l Co. v. United States*, 121 Fed. Cl. 428 (2015).

365. Freyfogle, *supra* note 125, at 453.

366. Christopher K. Odinet, *Banks, Break-ins, and Bad Actors in Mortgage Foreclosure*, 83 U. CIN. L. REV. 1155, 1160 (2015).

367. David Reiss, *The Federal Government's Implied Guarantee of Fannie Mae and Freddie Mac's Obligations: Uncle Sam Will Pick up the Tab*, 42 GA. L. REV. 1019, 1033 (2008). The balance sheets of these government-sponsored enterprises (the "GSEs," as they are called) were laden with toxic mortgage-backed securities and collateralized debt obligations that greatly called into question the ability of the two entities to continue to function. *See* Odinet, *supra* note 366, at 1171–72.

368. The credit default swap, derived from concepts found in the previously more common interest rate and foreign currency swaps, allowed investors to

In order to deal with these failing but systemically important entities, Congress essentially took them over through a series of legal transactions.<sup>369</sup> First, Fannie Mae and Freddie Mac were placed into conservatorship under the auspices of its regulatory supervisor, the Federal Housing Finance Agency (“FHFA”).<sup>370</sup> Federal bailout funds were used by the Treasury Department to purchase many of the toxic assets held by Fannie Mae and Freddie Mac in order to help them achieve a healthier balance sheet.<sup>371</sup> In exchange, the FHFA banned the entities from issuing any further dividends to its shareholders, removed both of them from the New York Stock Exchange, forced them to deliver to the Department of the Treasury a large number of shares of preferred stock (totaling a combined amount of \$189.5 billion), and lastly required that both Fannie Mae and Freddie Mac agree that all of their net profits for each quarter of the year would be immediately turned over to the U.S. Treasury.<sup>372</sup>

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make bets regarding credit events with reference to certain financial products (typically residential mortgage-backed securities (“RMBSs”), collateralized debt obligations (“CDOs”), and synthetic CDOs). See John Carney, *Here’s the Untold Story of How AIG Destroyed Itself*, BUS. INSIDER (Mar. 3, 2010, 9:22 AM), <http://www.businessinsider.com/heres-the-untold-story-of-how-aig-destroyed-itself-2010-3>. In essence, these contracts mimicked the effects of an insurance agreement (although they were not subject to insurance requirements such as the maintenance of certain capital reserves and an insurable property interest). Kristin N. Johnson, *Things Fall Apart: Regulating the Credit Default Swap Commons*, 82 U. COLO. L. REV. 167, 169–70 (2011); Frank Partnoy & David A. Skeel, Jr., *The Promise and Perils of Credit Derivatives*, 75 U. CIN. L. REV. 1019, 1049–50 (2007). Many traders and funds entered into credit default swaps with AIG in the run-up to the crash, often betting that there would be a default on any number of derivatives and securities. William K. Sjostrom, Jr., *The AIG Bailout*, 66 WASH. & LEE L. REV. 943, 954–55 (2009). AIG, for its part, readily entered into these contracts, even though the referenced obligations (specifically in the mortgage context) had zero underwriting and were highly likely to fail as the housing bubble burst. *Id.* at 959. When the inevitable occurred in 2008, AIG was called upon to pay up by the various counterparties to these swap contracts. See *id.* at 960–61. Although the company had a little more than \$1 trillion in assets in the run-up to the crisis, it was nowhere near positioned to make good on the payments it owed to these swap contract holders. *Id.* at 946 (“As of December 31, 2007, AIG had total assets of \$1.06 trillion, shareholders’ equity of \$95.8 billion, and a market capitalization of \$150.7 billion.”). Because AIG’s products had reached so far and wide into the American economy, its bankruptcy was predicted to be disastrous. See *id.*

369. Odinet, *supra* note 366, at 1157.

370. David Reiss, *An Overview of the Fannie and Freddie Conservatorship Litigation*, 10 N.Y.U. J.L. & BUS. 479, 479, 482 (2014).

371. See Odinet *supra* note 366, at 1172–73; Gretchen Morgenson, *Fannie, Freddie and the Secrets of a Bailout with No Exit*, N.Y. TIMES, FAIR GAME (May 20, 2016), [http://www.nytimes.com/2016/05/22/business/how-freddie-and-fannie-are-held-captive.html?\\_r=1](http://www.nytimes.com/2016/05/22/business/how-freddie-and-fannie-are-held-captive.html?_r=1).

372. See Reiss, *supra* note 370, at 492.

With regard to AIG, in order to save that entity from collapse and an ultimate bankruptcy, the Federal Reserve Bank of New York (“FRBNY”) made a loan of \$85 billion.<sup>373</sup> In exchange for this loan, the FRBNY obtained a majority and controlling number of shares in the company.<sup>374</sup> It was argued by market commentators at the time that without such measures, “ultrasafe money-market funds owned by individual investors to complex derivatives used by Wall Street banks” would crash.<sup>375</sup>

In both cases, these companies were in tremendous financial distress and, moreover, the financial health of these entities had become so intertwined with the financial health of the country that a failure of any one of them would have had dire consequences.<sup>376</sup> However, these entities were private companies and each had their own private shareholders.<sup>377</sup> Because the federal government required that a significant amount of the control and economic rights of these shareholders be suppressed in exchange for federal aid, many of them asserted constitutional takings claims.<sup>378</sup>

Professor Nestor Davidson explained that in 2013 and 2014 groups of GSE shareholders initiated lawsuits against the government, arguing that, among other things, the FHFA’s orders regarding the sweeping of net cash, the cessation of dividends, and the removal of the entities from the publicly traded marketplace constituted an unconstitutional taking of their property rights.<sup>379</sup> While, as Davidson notes, that litigation is still ongoing, to date courts have held that the actions taken by the FHFA with regard to Fannie Mae and Freddie Mac do not, in fact, amount to a taking of property rights.<sup>380</sup>

The reason behind many of these courts’ decisions hint at a larger move toward embracing the progressive property movement’s idea “that private ownership . . . is a tool that society uses to promote its interests.”<sup>381</sup> For instance, the court in *Perry Capital LLC v. Lew*<sup>382</sup> noted that while it is true that the FHFA foreclosed the possibility of dividend payments to shareholders (other than the

373. Sjostrom, *supra* note 368, at 963.

374. *See id.* at 976.

375. Monica Langley et al., *Bad Bets and Cash Crunch Pushed Ailing AIG to Brink*, WALL ST. J., <http://www.wsj.com/articles/SB122169421247449935> (last updated Sept. 18, 2008, 11:59 PM).

376. *See id.*

377. *Id.*

378. *See generally* Nestor M. Davidson, *Resetting the Baseline of Ownership: Takings and Investor Expectations After the Bailouts*, 75 MD. L. REV. 722 (2016) (giving in-depth analysis to the constitutional, property-related claims stemming from the GSE and AIG bailouts).

379. *See id.* at 731.

380. *Id.* at 735–36.

381. *See* Freyfogle, *supra* note 125, at 453.

382. 70 F. Supp. 3d 208 (D.D.C. 2014).

treasury) in the near term, the fact that these investors had purchased stock in private entities that were widely known to be highly regulated by the federal government makes the fact that dividend payments had ceased even more foreseeable and reasonable, and thereby less evident of a deprivation of the investors' "reasonable investment-backed expectations."<sup>383</sup> This idea of an investor operating in an arena that is inherently public and attuned to societal policy shifts—thereby imbuing such property rights with societal concerns—underscores Freyfogle's assertion that "[t]here is no need to weigh public interests against private interests in a kind of apples *versus* oranges assessment. The public interest is central, and private rights exist to the extent their recognition helps promote that public interest."<sup>384</sup>

A similar fate met the plaintiff-shareholders in the takings suits brought in connection with the AIG intervention.<sup>385</sup> In one such case, one of the company's largest shareholders filed suit against the government arguing that, although the FRBNY may have had the authority to make the loan under the company's then state of financial exigency, it did not have the authority to require stock in exchange for such credit and thereby become the controlling shareholder.<sup>386</sup> The company's largest shareholder alleged that this was an illegal act, and the government had effectuated a taking of the shareholders' property rights in the company.<sup>387</sup> The court in *Starr International Co. v. United States*<sup>388</sup> agreed with the plaintiff, who filed this class action on behalf of itself and other shareholders, that the FRBNY had acted beyond its authority when it took an equity stake in the company in exchange for the loan, but the judge nevertheless denied that a taking had occurred.<sup>389</sup> Importantly, the court stated that there had been no damage as a result of the FRBNY's act, due to the fact that without the loan, the shareholders (while certainly free of interference with their economic and governance rights in AIG) would have held merely worthless paper in the company.<sup>390</sup>

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383. *Id.* at 245 ("There can be no doubt that the plaintiff shareholders understood the risks intrinsic to investments in entities as closely regulated as the GSEs, and, as such, have not now been deprived of any *reasonable* investment-backed expectations.").

384. Freyfogle, *supra* note 125, at 453.

385. See Davidson, *supra* note 378, at 734–35.

386. See *id.* at 733–34.

387. *Id.* at 733.

388. 121 Fed. Cl. 428 (2015).

389. *Id.* at 434–35.

390. See *id.* at 436. This argument is similar to that adopted by the Supreme Court in *Faitoute Iron & Steel Co. v. City of Ashbury Park*, 316 U.S. 502 (1942), which involved a challenge to a New Jersey municipal rehabilitation law under the Contracts Clause. *Id.* at 507. The Court held that the bonds of the insolvent municipality were worthless, and therefore the law could not have

The court noted that “[i]n the end, the Achilles’ heel of Starr’s case is that, if not for the Government’s intervention, AIG would have filed for bankruptcy.”<sup>391</sup> If such an insolvency proceeding had been commenced, the court noted, then “AIG’s shareholders would most likely have lost 100 percent of their stock value.”<sup>392</sup> In other words, the shareholders of AIG, for all practical purposes, had property rights that were worthless as the company faced immediate insolvency and ruin.<sup>393</sup> Therefore, having “lost” some of those rights by virtue of the FRBNY’s exchange of the loan for the stock did not amount to a taking because the shareholders were at least better off after than they would have ever been before.<sup>394</sup>

The *Starr International* decision accentuates another important point about why a broader view of property rights in the context of public insolvency proceedings is important—property rights should not be mechanically enforced in a way that is meaningless and renders their value hallow. Davidson notes that “[t]he issue of the reasonableness of investor expectations must be evaluated not as a general matter, but in light of the relevant type of firm and the nature of the economic ownership” at issue.<sup>395</sup> He notes that Supreme Court jurisprudence has always held that takings cases should not be viewed in the abstract—rather, a taking is only compensable when there has actually been some sort of economic harm incurred.<sup>396</sup> Indeed, he explains that there is something particular about takings claims related to the interests of right holders in or against economically distressed companies<sup>397</sup>—a theory that should be extended to bondholders in connection with economically distressed governments, like Puerto Rico. The idea, as Freyfogle states, is not that “property exists chiefly to benefit the owner” but rather that courts should have “greater discretion to consider all relevant factors before allowing owners to enforce their

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practically impaired the obligation of the contracts. *See id.* at 513–16. This case was, however, partially overruled by *Puerto Rico v. Franklin California Tax-Free Trust*, 136 S. Ct. 1938 (2016), under the theory that, regardless of contracts clause limitations, states are prohibited from creating their own insolvency regimes due to the preemptive effects of federal bankruptcy law. *See id.* at 1945 (“In *Faitoute*, the Court held that federal bankruptcy laws did not pre-empt New Jersey’s municipal bankruptcy scheme, which required municipalities to seek relief under state law before resorting to the federal municipal bankruptcy scheme (citation omitted). To override *Faitoute*, Congress enacted [11 U.S.C. § 903(1),] expressly pre-empting state municipal bankruptcy laws.”).

391. *Starr Int’l*, 121 Fed. Cl. at 436.

392. *Id.*

393. *Id.*

394. *Id.*

395. Davidson, *supra* note 378, at 736.

396. *Id.* at 735.

397. *See id.* at 737.

rights.”<sup>398</sup> This is the very notion of social property—not that the government necessarily owes certain minimum standards to its people. A person’s property rights ought to incorporate the broader claims of others to basic human needs. Therefore, a proper vision of property law that allows for all types of property rights (secured and unsecured debt) to be modified as circumstances require—and as social property claims demand—permits courts to see social relations and “to consider the plight of people on the margins before enforcing property rights mechanically.”<sup>399</sup>

Further, although not within the realm of takings law, the Supreme Court’s jurisprudence in the context of the Contracts Clause<sup>400</sup> also embraces the notion that states can impair contract rights when the public need so dictates.<sup>401</sup> Similar to the Takings Clause, the general purpose of the Contracts Clause, as articulated by courts and scholars, is to prevent governmental interference with property rights.<sup>402</sup> The provision is meant “to encourage trade and credit by promoting confidence in the stability of contractual obligations.”<sup>403</sup> Because of the similarities in purpose and the overlap one often sees in the jurisprudence, it is helpful to understand how the Supreme Court has similarly shown a willingness to embrace progressive property concepts in the Contracts Clause arena as well.

Similar to the Takings Clause, the mandates of the Contracts Clause are not so rigid and unbending as the text would seem to indicate.<sup>404</sup> One of the most noted and contemporary U.S. Supreme Court decisions dealing with the Contracts Clause in the context of municipal debt is the 1977 decision in *United States Trust Co. v. New Jersey*.<sup>405</sup> In that case, involving a dispute between the bondholders of the Port Authority of New Jersey and New York on the one side and the legislature of both states on the other, the bondholders argued that the repeal of a statutory covenant on which they had relied when purchasing port authority debt violated the

398. See Freyfogle, *supra* note 125, at 453.

399. *Id.* at 452.

400. U.S. CONST. art. I, § 10, cl. 1 (“No State shall . . . pass any . . . Law impairing the Obligation of Contracts.”).

401. Brenner M. Fissell, Note, *The Dual Standard of Review in Contracts Clause Jurisprudence*, 101 GEO. L.J. 1089, 1091–92 (2013). I thank Professor Ronald J. Krotoszynski for suggesting this helpful comparison to the Contracts Clause jurisprudence and literature.

402. Henry N. Butler & Larry E. Ribstein, *State Anti-Takeover Statutes and the Contract Clause*, 57 U. CIN. L. REV. 611, 613, 624 (1988); Michael W. McConnell, *Contract Rights and Property Rights: A Case Study in the Relationship Between Individual Liberties and Constitutional Structure*, 76 CALIF. L. REV. 267, 278–80 (1988).

403. *U.S. Tr. Co. of New York v. New Jersey*, 431 U.S. 1, 15 (1977).

404. See *Ogden v. Saunders*, 25 U.S. 213, 353–54 (1827).

405. 431 U.S. at 27.

Contracts Clause.<sup>406</sup> In discussing the merits of the claim, the Court held that “[t]he Contract Clause is not an absolute bar to subsequent modification of a State’s own financial obligations.”<sup>407</sup> Rather, “an impairment may be constitutional if it is *reasonable and necessary to serve an important public purpose*.”<sup>408</sup>

The “reasonable and necessary” standard has a number of jurisprudential features that embrace the concepts expressed in the progressive property scholarship and should inform the Court in its Takings Clause analysis of public debt. For instance, the Supreme Court has noted that in determining whether the actions taken by a state governmental entity are constitutionally reasonable, “the inherent police power of the State ‘to safeguard the vital interests of its people’” must be borne in mind.<sup>409</sup> To that end, “the Contract Clause must be accommodated to the police power a state exercises to protect its citizens.”<sup>410</sup> Admittedly, “[t]he intersection of the state’s police power and the protections of the Contract Clause . . . presents difficult terrain. It requires a careful balancing of the contractual rights of the individual with the state’s inherent power to ensure the welfare of its citizenry.”<sup>411</sup> This balance, between individual property entitlements and the welfare of individuals strikes at the heart of progressive property theory.

In thinking about how a progressive account of property law can lead to a better allocation of rights in bankruptcy, it is important to note the inherent public nature of a sovereign debt crisis. Those who purchase government debt—for instance, those who purchase Puerto Rico’s debt—do so with the implicit understanding that they have entered a highly political environment.<sup>412</sup> Governments

406. *Id.* at 3, 9–10 (quoting (1962 N.J. Laws, c. 8, § 6 and 1962 N.Y. Laws, c. 209, § 6) “The 2 States covenant and agree with each other and with the holders of any affected bonds, as hereinafter defined, that so long as any of such bonds remain outstanding and unpaid and the holders thereof shall not have given their consent as provided in their contract with the port authority, (a) . . . and (b) neither the States nor the port authority nor any subsidiary corporation incorporated for any of the purposes of this act will apply any of the rentals, tolls, fares, fees, charges, revenues or reserves, which have been or shall be pledged in whole or in part as security for such bonds, for any railroad purposes whatsoever other than permitted purposes hereinafter set forth.”).

407. *Id.* at 25.

408. *Id.* (emphasis added).

409. *Energy Reserves Grp., Inc. v. Kan. Power & Light Co.*, 459 U.S. 400, 410 (1983) (quoting *Home Bldg. & Loan Ass’n v. Blaisdell*, 290 U.S. 398, 434 (1934)).

410. *Sanitation & Recycling Indus., Inc. v. City of New York*, 107 F.3d 985, 992 (2d Cir. 1997); *see also* *Allied Structural Steel Co. v. Spannaus*, 438 U.S. 234, 241–42 (1978).

411. *Buffalo Teachers Fed’n v. Tobe*, 446 F. Supp. 2d 134, 150 (W.D.N.Y. 2005).

412. *See* Jacob D. Charles, Note, *The Debt Limit and the Constitution: How the Fourteenth Amendment Forbids Fiscal Obstructionism*, 62 DUKE L.J. 1227, 1228–30, 1256–59 (2013).

operate in a democratic ecosystem where the interests of the people factor prominently in the decisions of public officials—including how property rights are determined.<sup>413</sup> That a public debt bondholder could not foresee that priorities might be adjusted in times of crisis represents a feigned ignorance that cannot and should not be used to frustrate the legitimate goal of restoring health to public finances. Indeed, if a government cannot engage in normal or even extraordinary measures to ensure the provision of essential public goods and services for its people then the sovereign power would mean very little. It is against these “background principles”<sup>414</sup> that Puerto Rico’s bondholders invested in the Commonwealth’s debt, and it is under these conditions that their “investment-backed expectations”<sup>415</sup> must be measured and judged.

### CONCLUSION

A rethinking of the way property rights are conceptualized in the context of public debt and insolvency proceedings, all within the larger framework of the Constitution, achieves a number of important goals. First, it ends the arbitrary way in which courts have treated the claims of different creditors (i.e., different property owners) by bestowing protections only on those who hold security and leaving all others out in the cold. It allows for disparate treatment only when disparate treatment is determined to be proper.

Second, it creates a more coherent and logical framework for the defining and protecting of property rights by creating uniformity in how the Takings Clause is interpreted, both inside and outside of bankruptcy proceedings. If debt is considered property, then it should always be considered property (for whatever that means)—even in insolvency proceedings. This helps avoid the development of competing and conflicting visions of what is owed to private owners when property rights are regulated.

Third, it removes a major impediment in the ability of Congress to exercise its reasoned judgment when deciding how best to resolve the public finance problems of governments in distress. By no longer having to construct a system that gives special, categorical treatment to a certain group of creditors over others, even when larger policy and social forces might call for a more varied result, lawmakers will have the flexibility to craft laws that are meaningful and better reflect the purpose of bankruptcy.

Fourth, such a refocused approach advances a more reasoned and organic view of the Constitution. Rather than placing insolvency law strictly within the ambit of the Bankruptcy Clause or

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413. *See id.* at 1235–36, 1260–62.

414. *Lucas v. S.C. Coastal Council*, 505 U.S. 1003, 1029 (1992).

415. *Perry Capital LLC v. Lew*, 70 F. Supp. 3d 208, 244 (D.D.C. 2014).

the Takings Clause, a progressive property account calls for a recognition that the two powers speak to one another and inform how the allocation of property rights are mediated in times of public financial distress.

Finally, it allows another opportunity to implement, in a tangible way, the principle that human values are inherently part of the property law question. Puerto Rico's debt crisis serves as a window through which we can see how these ideas play out in actual terms. As a matter of principle, Puerto Rico needs the authority to deal with its debt crisis. The basic framework of that authority and its process should facilitate the fair treatment of the property and human dignity concerns of all sides. An orderly and just restructuring scheme can be flexible without either offending constitutional claims to property or jettisoning human values.

If property and law are born together and must die together—and if debt is property—then debt and law do just the same. They live and operate together, constantly cognizant of the human story. Indeed, the significance of this relationship is particularly powerful in cases of public financial distress. The cost of failing to maintain this marriage of values is not measured in bond documents, contracts, or abstract theories—but in human lives.

Some debts are just not worth paying.

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