Constitutional Problems Associated with Dodd-Frank Title II

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Mr. Chairman and Members of the Committee:

Thank you for the opportunity to appear before you today to discuss constitutional problems associated with the Dodd-Frank Act. My comments are directed to Title II of the Act, which establishes a new "Orderly Liquidation Authority" for systemically significant financial firms. This authority is designed to create a new bankruptcy regime for systemically important financial companies that will eliminate the need for taxpayer bailouts of financial firms deemed too big to fail.

I am currently completing an article, coauthored with Margaret Merrill, addressing the constitutional issues raised by Title II. I have included a copy of the current draft of this article as an appendix to this statement. The article considers both the substantive constitutional issues presented by Title II as well as the procedural impediments the statute creates for getting these issues before a court.

The fundamental point I would make is this. Dodd Frank Title II, as presently written, raises some serious constitutional questions. Anyone opposed having a financial firm liquidated under Title II – this could be a director or officer of the firm, or a creditor of the firm – would have a strong incentive to raise these constitutional objections as a way of stopping the resolution process. Given the novelty and complexity involved in evaluating these objections, this would almost certainly lead to delay and confusion, undermining the purpose and efficacy of Title II. So I strongly urge the Congress to amend the statute to fix the constitutional problems, if Title II is to have a chance of delivering on its promises.

Fortunately, most of the constitutional problems can be fixed without performing radical surgery on the statute. The critical fix is to amend the law to adopt the original House version for commencing a liquidation of a financial firm, rather than the Senate version that was ultimately approved by the Conference Committee. Briefly put, the House version called for administrative appointment of the FDIC as receiver of a distressed systemically significant financial firm, followed by a right to go to court to have the appointment of the receiver set aside. You can call this ex post judicial review. While the Senate version required the same administrative findings, it also required that the appointment of the FDIC as receiver be formally made by the D.C. District Court. You can call this ex ante judicial review.

Ordinarily, there is nothing wrong with ex ante judicial review; indeed, it can offer greater protection against government abuse than ex post review. But in the context of the failure of a systemically significant financial firm, the Senate recognized that you could not have anything resembling an ordinary judicial trial before appointing a receiver. The publicity and delay would trigger the very financial panic that the orderly liquidation process is designed to prevent.

So what did the Senate do? It tightly constrained the ex ante judicial review. The court proceedings are held in camera – "on a strictly confidential basis." Only the financial firm is informed about the petition to appoint a receiver; other interested parties like employees, creditors, and counterparties are kept in the dark. Indeed, anyone disclosing the pendency of the court proceedings is subject to criminal prosecution. The court has only 24 hours to rule on the petition. It may consider only two out of seven determinations that must be made to commence a receivership. It can review these determinations only under a highly deferential "arbitrary and capricious" standard. And if the court fails to rule within 24 hours, the petition is deemed automatically granted. There can be no stay of the receivership pending appeal.

In other words, the Senate's version of ex ante review – which is the version currently incorporated in the statute – seeks to draw upon the authority of the federal courts before ordering the liquidation of a systemically significant financial firm. But in order to do so while also preserving the need for speed and confidentiality – not to mention the discretion of the executive branch in deciding whether to commence an orderly liquidation – it requires the court to act in a very un-judicial manner. The combination of ex ante review with no notice to stakeholders, 24 hours to make a decision, and tight constraints on the issues that can be considered, creates several serious constitutional problems.

Perhaps the most obvious is due process. Due process does not always require notice and a hearing before someone is deprived of their property. Various emergency situations like a health threat – or a threat of a financial crisis – may allow the government to act in a summary fashion. But if notice and a fair hearing are not made available before the deprivation takes place, the law is crystal clear that there must be notice and a fair hearing promptly afterwards. Dodd Frank, as enacted, provides for a hearing before rather than after the deprivation, but it truncates the notice and the hearing to the point where they are effectively meaningless. I cannot imagine that the Supreme Court would hold that the government can order the mandatory liquidation of a major financial firm without any meaningful notice to affected persons or any opportunity to contest the government's decision before or after the process gets started.

A related problem is Article III of the Constitution. Dodd Frank, not to put too fine a point on it, effectively requires the federal courts to rubber stamp the executive decision to commence an orderly liquidation process. The court gets 24 hours to rule on what is likely to be a highly complex and contested matter, and then is told it must apply a very deferential standard of review and must ignore five of the seven legal determinations that the executive must make before commencing the liquidation process. The courts will not take kindly to being conscripted to act in a manner inconsistent with the proper exercise of the judicial power.

A third problem is the First Amendment. Dodd Frank says you can be sent to jail for up to five years for disclosing the truth about a civil case brought against you by the government. There are of course a variety of circumstances in which judicial proceedings can be kept confidential. But they all involve the consent of the parties involved or preliminary determinations subject to reversal in later proceedings. Dodd Frank requires that once a receiver is appointed by the court, the firm must be liquidated, shareholders must be wiped out, directors must be dismissed, responsible officers fired. The appointment of the receiver is the last act by a court before all these consequences inevitably follow. And it is crime to disclose this to the world. Such a gag rule is unprecedented, and I think would be viewed very skeptically by the courts.

All these problems could be avoided by eliminating the Senate provision for ex ante review and restoring the House provision for ex post review. With ex post review, you can have administrative appointment of the receiver, preserving the confidentiality and the speed necessary to forestall a run on the financial company and the ensuing financial panic. The receiver can immediately stay all collection actions and preferential transfers and more importantly assume or transfer time sensitive qualified financial contracts. All interested parties can then be promptly notified, and any party interested in challenging the appointment of the receiver can do so in court, without any limitation on the issues presented, the standard of review, or the time the court takes to sort out the issues and reach a decision.

Such ex post review, by affording notice and an opportunity for a full and fair hearing after the appointment of a receiver, eliminates the due process problem. It eliminates the Article III problem, because the court would be asked to act in a manner fully consistent with the judicial function. And it eliminates any need for a gag rule, and hence any First Amendment deficiencies.

It is probably true, as a practical matter, that once a receiver is appointed a reviewing court will be reluctant to unwind the process. But the very availability of such ex post review would act as an important safeguard against executive abuse. Making such robust review available would serve to constrain the executive to exercise the vast power bestowed on it in a responsible manner. As such, it would not only eliminate the constitutional problems I have highlighted, but would also provide far more protection for individual rights than Dodd Frank does in its current incarnation.

I thank the Committee for its attention and will be glad to answer any questions.

Appendix

DODD-FRANK ORDERLY LIQUIDATION AUTHORITY: TOO BIG FOR THE CONSTITUTION?

Thomas W. Merrill*
Margaret L. Merrill**

Introduction

The Dodd-Frank Act[1] is in significant part a response to public outcry over public bailouts of financial firms that are deemed too big to fail. In the financial crisis of 2008-09, the federal government supplied emergency financial support to many financial firms in order to keep them afloat. The fear was that the insolvency of one or more of these firms would trigger a chain reaction by creditors, analogous to a run on the bank, which would in turn have ripple effects throughout the economy. As it happened, the financial system did freeze up for a short time after the Lehman Brothers bankruptcy,[2] which tipped the economy into a deep recession followed by a painfully weak recovery.[3]

Once the immediate crisis subsided, many perceived that large financial firms and their well-paid officers and directors had survived nicely, whereas large numbers of ordinary Americans were suffering from the lingering effects of the downturn. The idea that the federal government would rescue large financial firms with taxpayer dollars, while ordinary citizens lost their jobs and watched their savings evaporate, has produced widespread voter anger. One proposition all politicians seem to agree upon, at least publicly, is that never again should ordinary folks be taxed to prop up giant financial firms deemed too big to fail by the government.[4]

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[1] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010) [hereinafter cited as DFA].

[2] The Orderly Liquidation of Lehman Brothers Holdings Inc. under the Dodd-Frank Act, FDIC Quarterly, Vol. 5, No. 2, 3-4 (2011) at http://www.fdic.gov/bank/analytical/quarterly/2011_vol5_2/Article2.pdf.

[3] The Restoring Financial Stability Act of 2010, S. Rep. No. 111-176, at 43- 44 (2010). ("When Lehman Brothers declared bankruptcy, the markets panicked and the crisis escalated. With no other means to resolve large, complex and interconnected financial firms, the government was left with few options other than to provide massive assistance to prop up failing companies in an effort to prevent the crisis from spiraling into a great depression. Despite initial efforts of the government, credit markets froze and the U.S problem spread across the globe. The crisis on Wall Street soon spilled over onto Main Street, touching the lives of most Americans and devastating many.")

[4] Amendment No, 689 to the Concurrent Budget Resolution on the Budget. Fiscal Year 2014, Con. Rec.

In terms of reform, there were a number of possible structural alternatives to public bailouts of financial firms deemed too big to fail. One would be to break up large financial firms, so that no single firm could be said to be too big to fail. This might be accomplished by imposing line of business restrictions, as under the Glass Steagall Act, with companies limited to one line of business, such as commercial banking, investment banking, brokerage, or insurance. Dodd-Frank's so-called Volker rule[5], which limits the ability of banks to engage in proprietary trading, is a limited version of this strategy. Or Congress could impose limits on the maximum assets of financial firms, with mandatory divestiture once the limit is reached. Downsizing presumably would reduce the risk of single rogue institution bringing the entire financial system down when risky bets turn bad.

Another structural solution would be to impose limits on the debt financial firms can take on, as by increasing capital reserve requirements or (in the case of nonbank firms) imposing them for the first time.[6] The higher the capital reserve requirements are, the lower the risk of insolvency, and hence the lower the need for future bailouts. Higher reserve requirements would of course reduce the profitability of the financial sector, which would presumably re-direct assets (and talent) to other sectors. From a social welfare perspective, the tradeoff might be worthwhile – lower profitability for financial firms in return for lower risk of future financial crises that afflict pain on millions of ordinary Americans.

A third structural solution, which has been advanced by bankruptcy scholars,[7] would be to amend the Bankruptcy Code to subject novel financial instruments like repurchase agreements (repos) and derivatives or swaps to the automatic stay and avoidance provisions of the Bankruptcy Code. Interestingly, the law had moved in exactly opposite direction before the financial crisis, with special legislation (pushed by the financial industry) exempting these novel

113th Congress (2013-2014) (Senate - March 22, 2013) (the unanimously approved amendment to the Democrats' doomed 2014 budget proposal, attempts to minimize the advantage that Dodd Frank otherwise bestows on big banks by eliminating subsidies or other funding advantages for Wall Street mega-banks with more than $500 billion in assets).

[5] See Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No.111–203, § 619, 24 Stat. 1376 (2010) (Dodd-Frank Act).

[6] The Basel Accords that regulate international commercial banks adopt this strategy. Under the recent Basel III Accords, , effective as of 2015, common equity that banks must keep on hand will increase from 2% to 4.5% of risk-weighted assets, and the so-called "Tier 1 ratio" will increase from 4% to 6%. As of 2019, banks will be required to add a further conservation buffer of 2.5% to both of these metrics. *See* Patrick Slovik & Boris Cournède, *Macroeconomic Impact of Basel III,* OECD Economics Department Working Papers, No. 844, OECD Publishing (2011) at *http://dx.doi.org/10.1787/5kghwnhkkjs8-en*.

[7] David A. Skeel & Thomas H. Jackson, Transaction Consistency and the New Finance in Bankruptcy, 112 Colum. L. Rev. 152 (2012); see also KENNETH E. SCOTT AND JOHN B. TAYLOR, BANKRUPTCY NOT BAILOUT: A SPECIAL CHAPTER 14 (2012) (urging the adoption of a new chapter of the Bankruptcy Code to deal with systemically significant financial firms).

instruments from resolution in bankruptcy.[8] Without the shield of the bankruptcy process, the logical response of counterparties to these instruments when they sense a financial firm is in distress is to race to cash out – exactly the kind of free-for-all that bankruptcy is designed to prevent. It is thus plausible that the special exemption from bankruptcy adopted for repos and swaps contributed if it did not cause Lehman's collapse and the panic that followed.[9] Subjecting these instruments to ordinary bankruptcy powers might solve the too big to fail problem, at least insofar as nonbank financial firms are concerned.

These structural solutions – any one of which could be implemented with a relatively simple piece of legislation – were rejected not because they are bad ideas but because they were adamantly opposed by the financial industry. Clearly, financial firms did not want to be downsized or de-leveraged. It is less clear why the financial industry opposed reforming the Bankruptcy Code to subject novel financial instruments to the automatic stay and avoidance provisions. But the conventional wisdom in the industry is that this would unduly interfere with the operation of the markets in which these instruments are bought and sold.[10] In any event, because each of these solutions faced concerned opposition from big finance, they were never seriously considered by the Treasury Department – which provided the initial draft legislation that became the Dodd Frank Act – or the Congress that adopted it. Firms that are too big to fail are too big to be challenged politically.

Given that these relatively straightforward structural solutions were off the table, how could the politicians square the circle between preventing future taxpayer bailouts of large financial firms while leaving the prerogatives of these firms essentially untouched? The answer is complicated, as revealed at once by looking at the immense length of the Dodd-Frank Act. Some of the measures in the Act are designed to improve the regulation of derivatives and other complex financial instruments thought to have been inadequately regulated before the financial crisis.[11] Others are designed to insure better advance warning of systemic financial risks.[12] Still others are designed to beef up consumer information and protection against overly-aggressive

[8] See Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA) (Pub.L. 109-8, 119 Stat. 23) at 11 U.S.C. §§ 362(b)(6), (7), (17); 546 (e)-(g); 555; 559; 560; also see Federal Deposit Insurance Reform Act of 2005 (Title II, subtitle B of Pub.L. 109-171, 110 Stat. 9), enacted February 8, 2006, with a companion statute, Federal Deposit Insurance Reform Conforming Amendments Act of 2005, Pub.L. 109-173, 119 Stat. 3601, enacted February 15, 2006).

[9] Skeel and Jackson, *supra* note 7, at 164-5.

[10] *Id.* at 159-162.

[11] *See* DFA, Title VII, §§ 701 -774, (the Wall Street Transparency and Accountability Act of 2010) and Title VIII, §§801-814 (Payment, Clearing, and Settlement Supervision)

[12] *See* DFA, Title I, Subtitle A, §§ 111 – 123 (Financial Stability Oversight Council)

lending and other banking practices.[13] But the fundamental decision not to tinker with the size or profitability of large financial firms, or to subject novel financial instruments to ordinary bankruptcy processes, created challenging design issues in achieving the fundamental objective of eliminating future taxpayer-funded bailouts of financially distressed firms.

The core of the legislative strategy, which is set forth in Title II of Dodd- Frank, is to replace taxpayer bailouts of systemically significant distressed firms with a kind of specialized bankruptcy process, which the Act labels "orderly liquidation." This specialized bankruptcy regime applies uniquely to bank holding companies and other systemically significant nonbank financial firms.[14] (Ordinary banks and savings and loans that take government-insured deposits were already subject to the resolution by receivership or conservatorship, and this authority includes provisions allowing the receiver to take systemic financial risk into account in certain circumstances.[15]) Under this new resolution authority, government agencies are given broad discretion to decide on a case-by-case basis that a large nonbank financial firm is in trouble and that its failure would pose a threat to the economy. This decision leads to a takeover of the firm by a government receiver, typically the Federal Deposit Insurance Corporation (FDIC),[16] which proceeds to run the company as it resolves claims of creditors until the firm is eventually liquidated. Positive-value assets can be transferred to a "bridge financial company" and eventually folded into another firm.[17] If financing is required to meet obligations while the firm

[13] *See* DFA, Title X, §§ 1001 – 1100H (Bureau of Consumer Financial Protection)

[14] There are four categories of financial companies that may be subject to the Title II Liquidation Authority under the DFA. The first category is bank holding companies. *See* DFA, Title II, §203(a)(1)(A), §201(a)(11)(i) and Title I, §102(a)(1). The second category is nonbank financial companies or more specifically companies with at least 85% of their gross revenue or consolidated assets derived from activities that are financial in nature or incidental to financial activity, including the ownership or control of one or more insured depository institutions. *See* DFA, Title II, §203(a)(1)(A), §201(a)(11)(ii)&(iii) and Title I, § 102(a)(4). The third category includes subsidiaries of the financial companies identified in first two categories, except for those subsidiaries that otherwise qualify as insured depository institutions or insurance companies. *See* DFA, Title II, §203(a)(1)(A) & §201(a)(11)(iv). The fourth category includes entities that qualify as brokers and dealers and are accordingly registered with the SEC and members of the SIPC. *See* DFA, Title II, §203(a)(1)(B)&(C) § 201(a)(7).

[15] The FDIC is charged with administering the resolution of failed or capital-deficient government-insured depositary institutions. The payment of deposits and other creditor claims by the FDIC is generally governed by the "least cost resolution rule". *See* 12 U.S.C. § 1823(a)(4)(A). Under certain circumstances, however, the FDIC is allowed to diverge from the priority scheme established by the least cost resolution rule. Specifically, if adherence to the rule would have serious adverse effects on financial stability, the FDIC is allowed to disregard least cost resolution rule and take alternative action in the name of mitigating these adverse effects, including making selective payments to non-depository creditors. *See* 12 U.S.C. § 1823(c)(4)(G).

[16] The Securities Investor Protection Corporation (SIPC) serves as a trustee under a receivership for covered brokers and dealers. DFA § 205.

[17] *See* DFA, Title II, §210(a)(1)(F) and §210(h). Specifically any bridge financial company can be used to assume the liabilities, purchase assets as well as perform any other temporary function which the FDIC is authorized to undertake in § 210(h). *Id.* at § 210(h)(B)(i),(ii)&(iii).

is wound down, the necessary funds will be supplied by the Treasury.[18] The Act nevertheless insists that this funding is not a bailout, because any deficiencies will be financed by wiping out shareholder equity, rejecting claims of unsecured creditors,[19] and, if need be, by imposing special ex post "assessments" on other large financial firms.[20]

In addition to its perceived unfairness, a policy of bailing out firms that are deemed too-big-to-fail is objectionable on the ground that it promotes excessive risk taking. When such a firm makes risky bets that pay off, the gains are captured by top level management and shareholders; but when the firm makes risky bets turn disastrous, the losses are borne by taxpayers.[21] This asymmetry creates a moral hazard of the heads-I-win-tails-you-lose variety. If permanently institutionalized, would likely give rise to too much risk taking by large financial firms.

Title II is supposed to put an end to this moral hazard.[22] The statute includes a number of punitive features designed to deter systemically significant financial firms from engaging in excessively risky behavior.[23] A distressed firm that goes through the Title II process must be "liquidated," its shareholders must be wiped out before creditors take a hit, its directors must be fired, and its officers who were "responsible" for the financial distress must be dismissed.[24] These provisions are designed to assure that the public will not immediately see a firm with the same name, and the same personnel, raking in millions shortly after the resolution process is over.

[18] *Id.* at §204(d) and §210(n)

[19] *Id.* at §204(a)(1)&(2). The FDIC, along with other applicable enforcement agencies, are also required to ensure "that all parties… having responsibility for the condition of the [failed] financial company bear losses consistent with their responsibility, including actions for damages, restitution, and recoupment of compensation and other gains not compatible with such responsibility." *Id*. at § 204(a)(3).

[20] *Id.* at §210(o); Conference Report on H.R. 4173 the Dodd-Frank Wall Street Reform and Consumer Protection Act, H. Rpt. 111-517, 11th Cong. 2d Sess. (2010) at 865-66.

[21] The problem is compounded by the fact that creditors of firms deemed too big to fail have little incentive to monitor the firm's behavior or to care whether the firm has a reputation for making prudent and sound and investment decisions. *See* Gary H. Stern and Ron J. Feldman, *Too Big To Fail: The Hazards of Bank Bailouts*, Brookings Institution Press, Washington, D.C., p. 17-19 (2004).

[22] The statute states that its basic purpose is "to provide the necessary authority to liquidate failing financial companies that pose a significant risk to the financial stability of the United States in a manner that mitigates such risk and minimizes moral hazard." DFA, § 204(a).

[23] The FDIC must remove the management and board of directors of any covered financial company it decides to unwind pursuant to Title II. *Id.* at § 206(4)&(5). It must also ensure that shareholders of the covered financial company do not receive payment until all other claims as well as the orderly liquidation fund (if such is in fact established) are paid in full. *Id.* at § 206(2).

[24] *Id.* at § 206(4)&(5).

Nevertheless, Title II's orderly resolution process preserves a version of taxpayer-funded socialization of losses. This is because the Treasury is authorized to advance funding to a firm undergoing resolution under Title II, and if, after wiping out shareholders and unsecured creditors, the proceeds obtained from selling the firm's assets are inadequate to reimburse the Treasury, the statute authorizes the Treasury to impose so-called "risk-based assessments" on other large financial firms in order to recoup these monies.[25] These assessments are a tax by any other name. Whether the incidence of this tax will be borne by the shareholders of the assessed financial firms or the public in the form of higher fees for financial services is impossible to determine; almost certainly some of both.[26] In any event, under Dodd-Frank Title II losses created by excessive risk-taking will be borne at least in part by ordinary taxpayers and citizens, as under the regime of bailouts now so widely condemned.

No one seems happy with the complicated compromise embodied in Title II. Small financial firms are aggrieved by the provisions that continue to provide an implicit subsidy for large financial firms, in the form of the socialization of losses in the event they fail. They argue that this implicit subsidy lowers the costs of borrowing to large firms relative to small firms, giving them an unwarranted competitive advantage.[27] Managers and investors of big financial firms are aggrieved by possibility that they will be wiped out if and when they get into trouble sometime in the future. Certainly those who wanted fundamental reform of the financial industry are dissatisfied with the statute's preservation of the essential attributes of the status quo.

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[25] DFA, § 210(n)(9).

[26] Tax incidence analysis reflects the well established idea that the entity or individual legally obligated to pay a tax often does not bear the full economic burden of the tax. This is especially true in situations where the taxpayer is able to pass the cost of the tax on to third parties through increased market prices. *See* Jacob Nussim, *The Recovery of Unlawful Taxes*, 28 Va. Tax Rev. 893, 901-902 (2009). A logical extension of this analysis is that the more monopoly power any taxpayer-entity has the more the taxpayer is able to shift the costs of any taxes assessed against it. In the case of any financial institution deemed too big to fail, their market power would suggest that at least some of the costs would be shifted to others.

[27] More recent studies have suggested that this advantage is indeed significant. *See* Kenichi Ueda and Beatrice Weder di Mauro, *Quantifying Structural Subsidy Values for Systemically Important Financial Institutions*, IMF Working Paper (May 2012) available at http://www.imf.org/external/pubs/ft/wp/2012/wp12128.pdf (finding that the subsidy to systemically important financial institutions created by the implicit expectation of state funded bailouts and otherwise embedded in these institution's credit ratings is as much as 80 basis points). "Small as it might sound, 0.8 percentage point makes a big difference. Multiplied by the total liabilities of the 10 largest U.S. banks by assets, it amounts to a taxpayer subsidy of $83 billion a year. To put the figure in perspective, it's tantamount to the government giving the banks about 3 cents of every tax dollar collected." *Why Should Taxpayers Give Big Banks $83 Billion a Year?,* Bloomberg (Feb 20, 2013) available at http://www.bloomberg.com/news/2013-02-20/why-should-taxpayers-give-big-banks-83-billion-a-year-.html.

In keeping with Tocqueville's famous adage that "[s]carcely any political question arises in the United States that is not resolved, sooner or later, into a judicial question,"[28] Dodd-Frank's orderly liquidation authority is now the subject of a lawsuit. Eleven state attorneys general have filed suit in the U.S. District Court for the District of Columbia charging that Title II violates due process, Article III of the Constitution, and the uniformity requirement of the Bankruptcy Clause.[29] On the merits, the contentions are surprisingly strong. Most of the constitutional infirmities in Title II stem from a decision to have the receiver for a systemically significant nonbank financial firm appointed by a federal district judge. In order to confer appointment authority on a federal judge, and yet also prevent the modern-day equivalent of a run on the bank, the statute prescribes a clandestine process in which the district judge is given 24 hours to rule on a petition to appoint a receiver; it prohibits the court from giving notice of the proceedings to creditors or other interested third parties; and it imposes criminal penalties on anyone who publicly discloses the pendency of the proceedings. Moreover, the hapless district judge is entitled to consider only two factual issues under a highly deferential standard of review in deciding whether to order the liquidation of a major financial firm, and is given only 24 hours to do so make the decision, otherwise the petition is deemed automatically granted. For good measure, the statute proscribes any stay pending appeal. In effect, the statute seeks to draw on the prestige of the federal courts in making the appointment of a receiver, while depriving parties with a vital stake in the matter of any notice or meaningful opportunity to be heard, and handcuffing the court from acting in a way that is consistent with judicial authority.

The statute also creates a specialized form of bankruptcy that gives the executive branch of the federal government broad discretion to subject some nonbank financial firms to this special insolvency regime leading to liquidation, while others go through ordinary bankruptcy, which includes the possibility of reorganization. Allowing the executive to pick and choose different resolution regimes for firms in the same industry based on necessarily subjective determinations of the impact of insolvency on "financial stability in the United States"[30] at least arguably violates the uniformity requirement of the Bankruptcy Clause.[31] And within the new regime of orderly liquidation, the statute gives a federal agency – typically the FDIC -- broad discretion to depart from the principle that all creditors of the same class should be treated

[28] Alexis de Tocqueville, DEMOCRACY IN AMERICA, 280 (Philips Bradley ed. 1980 (1835).

[29] State National Bank of Big Spring v. Wolin, United States District Court for the District of Columbia, No. 1:12-cv-01032 (as amended Feb. 19, 2013) (hereafter "*Big Spring 2nd Amended Complaint*"). The eleven states are Alabama, Georgia, Kansas, Michigan, Montana, Nebraska, Ohio, Oklahoma, South Carolina, Texas and West Virginia.

[30] DFA § 203(b)(3)

[31] The Constitution authorizes Congress to establish "*uniform* Laws on the subject of Bankruptcies throughout the United States." U.S. Const. art I, § 8, cl. 4 (emphasis added).

equally.[32] This too arguably contradicts violates received understandings of uniformity in the bankruptcy context.

These constitutional infirmities could easily have been avoided. Ordinary bank receiverships are commenced by an executive appointment of a receiver, followed by a right of plenary judicial review – a process that allows all affected interest holders to challenge the appointment of a receiver after-the-fact, and permits the reviewing court to function in an appropriate judicial manner. This kind of ex post judicial review is undoubtedly constitutional in the context of a statutory regime designed to prevent a financial crisis. In fact, the Administration's proposed legislation, and the House bill, called for a process for appointing a receiver closely modeled on the bank receivership model. For unexplained reasons, however, the Senate rejected this model, and substituted the provisions that ended up in the legislation, calling for judicial appointment of a receiver coupled with draconian limitations on the authority of the court that render the judicial process virtually meaningless. Thus, the constitutional infirmities associated Title II's provisions for appointment of a receiver could fixed simply by amending the statute to incorporate the House provisions on appointment, rather than the substitute insisted upon by the Senate.

Whether the arguable violations of the uniformity requirement of the Bankruptcy Clause could be fixed is harder to say. The central objective of Title II is to give the government a new tool to avoid bailouts or government takeovers of troubled financial firms. Whether such authority can be cabined by predictable rules laid down in advance is debatable. However, the loosely-written provision allowing the FDIC to depart from equal treatment of similarly-situated creditors[33] could almost certainly have been drafted more narrowly. Of course, in today's legislative environment, obtaining these kinds of legislative fixes is may be impossible. Which means the issues may have to be confronted by a court.

We begin by examining the two statutory models for initiating resolution authority that served as a backdrop to the Dodd-Frank Act – bank receivership law and bankruptcy – and summarize the ways in which Dodd-Franks' Title II deviates from both models. We then consider various legal avenues for raising a constitutional challenge to Title II, each of which is problematic. Part III analyzes the due process and Article III objections to Title II in greater detail, including possible strategies for avoiding these difficulties. Part IV turns to the potential constitutional issues under the Bankruptcy Clause and the First Amendment. Part V lists some

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[32] DFA § 210(b((4). Departures from equal treatment are authorized if the FDIC determines that this "is necessary" to maximize the value of the liquidated company's assets, continue essential operations, maximize the value of the sale of assets, or minimize losses on the sale of assets. Id. There is no provision for judicial review of such a determination.

[33] DFA § 210(b(4)).

possible takings issues, and provides an analysis of how impairment of security interests might be analyzed under the Takings Clause. A brief conclusion follows.

I. Title II's Orderly Liquidation Authority

Title II of the Dodd-Frank Act sets forth a new "Orderly Liquidation Authority" (OLA) designed to serve as a substitute for future government bailouts of financial firms deemed too big to fail, in the sense that resolution of their affairs under ordinary bankruptcy law or other insolvency laws would threaten the stability of the financial markets. Lehman Brothers is the obvious object lesson here.[34] To avoid financial panic or various contagions analogous to a run-on-the-bank, the statute assumes that the resolution of these systemically-significant firms must occur rapidly and without any advance public notice. Thus, the process of appointing a receiver must occur "on a strictly confidential basis" without any public disclosure.[35] The Administration proposal and the House bill sought to achieve expedition and confidentiality by having the Secretary of the Treasury appoint a receiver, subject to ex post judicial review. The Senate decided at the last minute that the receiver should be appointed by a judge. In order to preserve speed and confidentiality, however, the Senate bill, which was the version enacted, prohibits public disclosure of the judicial proceeding and gives the court designated to appoint the receiver only 24 hours in which to rule.[36] This clandestine process deprives stakeholders of any notice of a process that must lead to liquidation of a major financial firm. And the extremely short deadline renders judicial oversight essentially meaningless, given the complexity of the matters involved. The Senate substitute is a classic example of an unforced legislative error, for it renders the statute vulnerable to constitutional challenge on due process, Article III, and First Amendment grounds.

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[34] *See Financial Regulatory Reform, A New Foundation: Rebuilding Financial Supervision and Regulation*, White Paper issued by the U.S. Department of the Treasury (June 17, 2009) available at http://www.hm-treasury.gov.uk/d/reforming_financial_markets080709.pdf. ("Treasury White Paper" hereafter) ("The federal government's responses to the impending bankruptcy of Bear Stearns, Lehman Brothers, and AIG were complicated by the lack of a statutory framework for avoiding the disorderly failure of nonbank financial firms, including affiliates of banks or other insured depository institutions. In the absence of such a framework, the government's only avenue to avoid the disorderly failures of Bear Stearns and AIG was the use of the Federal Reserve's lending authority. And this mechanism was insufficient to prevent the bankruptcy of Lehman Brothers, an event which served to demonstrate how disruptive the disorderly failure of a nonbank financial firm can be to the financial system and the economy.")

[35] DFA, § 202(a)(1)(A)(iii).

[36] "If the Court does not make a determination within 24 hours of receipt of the petition – (I) the petition shall be granted by operation of law; (II) the Secretary shall appoint the Corporation as receiver; and (III) liquidation under this title shall automatically and without further notice or action be commenced and the Corporation may immediately take all actions authorized under this title." *Id.* at § 202(a)(1)(A)(v).

The OLA process may never be used. It may remain the proverbial musket in the closet that the government holds in reserve while arranging workouts with creditors or sales or mergers of the troubled firm in lieu of "orderly liquidation."[37] If used, the OLA process may not be contested. The statute specifically invites the directors of a troubled financial firm to consent to OLA, and dangles a carrot in front of directors in the form of promised immunity from any action by shareholders or creditors for "acquiescing in or consenting in good faith to the appointment of the Corporation as receiver."[38] It would take an intrepid director to do battle with the Executive Branch over the fate of a financially troubled firm, knowing that any diminution in financial value attributable to delay could be challenged in future litigation by disgruntled creditors and shareholders, whereas capitulation to the government will result in immunity.

In any event, whether the OLA authority is used or merely threatened, the credibility of the government to use the new procedure will depend importantly on whether the relevant actors perceive this authority to be constitutional. As we shall see, there are several features of Title II that give rise to serious questions on this score.

The basic model for the OLA process is existing law providing for administrative receiverships of FDIC-insured banks. Dodd-Frank takes this bank receivership law and adds to it a number of provisions borrowed from the Bankruptcy Code, which is essentially a judicially-supervised resolution process. As a result, the OLA is an administrative rather than a judicial resolution process, but one that hews more closely to the substantive law of bankruptcy than it does to the substantive law that governs bank receiverships. Many of the constitutional issues raised by Title II stem from the unique provisions that govern the appointment of a receiver under the OLA. These provisions do not follow the template of either bank receivership law or bankruptcy law. Rather, they were adopted by the Senate during the final days of intense negotiation in the Senate over what became the final form of law. Accordingly, we begin with a brief review of the benchmarks established by bank receivership and bankruptcy law, and trace the evolution of the provisions prescribing how an OLA is commenced in the legislative history of Dodd-Frank.

A. Bank Receiverships and Bankruptcy

By way of background, it will be helpful to say a few words about two existing forms of resolution authority – bank receiverships and bankruptcy – and in particular how they are commenced and the extent to which judicial review is available under each form.

[37] David Skeel, The New Financial Deal: Understanding the Dodd-Frank Act and Its (Unintended) Consequences 139-40 (2011).

[38] DFA, § 207.

Under current practice, banks that become financially distressed are nearly always put into a receivership in which the Federal Deposit Insurance Corporation (FDIC) acts as receiver exercising powers under federal law.[39] It is theoretically possible for state-chartered banks to have a state-appointed receiver, but the FDIC can take over a state receivership if the bank has FDIC-insured deposits, which virtually all banks do.[40] The statutes require either that the FDIC be appointed as receiver by the relevant bank supervising agency (such as the Office of the Comptroller of the Currency in the case of a federally-chartered bank)[41] or that the FDIC appoint itself as receiver if the assets of the federal deposit insurance fund are at risk.[42] Once the FDIC assumes control of the bank as receiver, the bank has a short period of time (typically 30 days) in which to commence an action in federal district court seeking an order dissolving the receivership.[43] The statutes authorizing this form of review include no limits on the issues the court may consider or the time the court may take in rendering a decision. Further, they appear to contemplate that the issues will be resolved on a record made by the court, since there will be no administrative record in the ordinary meaning of the term for the court to review. In other words, judicial review occurs after the receivership is commenced and is de novo as to both fact and law.[44]

What actually happens in a bank receivership, according to recent descriptive accounts, is roughly as follows.[45] The appropriate bank regulatory authority (state or federal) sends the FDIC

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[39] Conservatorships are also authorized by law, but are rarely used. The basic difference is that under a receivership the bank's charter is revoked and its assets and liabilities are transferred to other banks or auctioned off; under a conservatorship the conservator takes control of the bank and reorganizes it so that it can resume operations under its existing charter.

[40] See 12 U.S.C. § 1821(c)(4), (5).

[41] See 12 U.S.C. § 1821(c)(2)(i) ("The Corporation may, at the discretion of the supervisory authority, be appointed conservator of any insured Federal depository institution and the Corporation may accept such appointment.")

[42] See 12 U.S.C. § 1821(c)(4) ("Notwithstanding any other provision of Federal law, the law of any State, or the constitution of any State, the Corporation may appoint itself as sole conservator or receiver of any insured State depository institution if…" certain findings (described in 12 U.S.C § 1821(c)(4)(A)&(B)) are made by FDIC in regards to the financial insufficiency of the insured State depository institution at issue.)

[43] 12 U.S.C. § 1821(c)(7). For any national bank the decision to appoint a receiver is to be determined by the OCC at the discretion of the Comptroller. 12 U.S.C. § 191. The OCC's decision to appoint a receiver is generally not subject to judicial review. United States v. Morgenthau, 85 F. 2d 811 (D.C. Circuit 1936), *cert. denied,* 299 U.S. 605 (1935). In addition to the grounds specified 12 U.S.C § 1821, the OCC may also appoint a receiver upon its conclusion that the bank's board of directors consists of less than five members. 12 U.S.C. § 191(2).

[44] *See* 12 U.S.C. § 1821(d)(13)(C) and (d)(13)(D).

[45] The following summary is drawn from Stanley V. Ragalevsky & Sarah J. Ricardi, Anatomy of a Bank Failure, 126 Banking L. J. 867 (2009); John L. Douglas and Randall D. Guynn, Resolution of US Banks and Other Financial Institutions 311-77, in Debt Restructuring (Rodrigo Olivares-Caminal et al eds., Oxford U. Press 2011); Federal Deposit Insurance Corporation, The Resolution Handbook (2003). See also David A. Skeel, Jr., The Law and Finance of Bank and Insurance Insolvency Regulation, 76 Tex. L. Rev. 723, 727-31 (1998).

a "failing bank letter," or the FDIC determines based on its own information that a bank is in distress. The FDIC then sends a "planning team" to the distressed bank to make a confidential assessment of its assets and liabilities. Based on this information, the FDIC develops an appropriate resolution strategy, most commonly a sale to another bank.[46] The FDIC puts together an information package about the bank, which is communicated to a list of potential bidders identified by the FDIC staff. These bidders sign confidentiality agreements and, if they wish, submit bids for the bank or its assets on a secure extranet site. FDIC officials evaluate the bids and recommend the least cost resolution to the FDIC Board. If the Board approves, the FDIC is officially appointed receiver. The appointment typically occurs on a Friday afternoon. Over the weekend, the bank is secured, its books are seized, the locks are changed, and signage is modified; the new bank opens for business on Monday morning.[47] Subsequently, creditors of the failed bank submit claims to the FDIC, which the agency resolves, giving priority to secured creditors and depositors.[48] Any creditor dissatisfied with the FDIC's resolution of its claim can bring an action in federal court seeking review of the agency's determination.[49] Such actions are occasionally brought, but they are rarely successful.[50]

Although judicial review of the decision to commence a receivership is expressly authorized by statute, banks rarely invoke this authority.[51] Indeed, the possibility of judicial review is so remote it is not even mentioned in recent descriptive accounts of bank receiverships. There are powerful practical reasons why banks would not seek ex post judicial review of the appointment of a receiver.[52] Once a receivership has commenced, courts are highly unlikely to

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[46] The disposition of a failing bank in this manner is often referred to as a purchase and assumption transaction ("P&A"), because the healthy bank selected by the FDIC agrees to purchases some portion of the failed bank's assets as well as assume some portion of the failed bank's deposit and other liabilities. *See* Ragalevsky & Ricardi *supra* at 877. P&A transactions made up 34 of the 40 resolutions that were carried out by FDIC from January 2000 through August 2008. *Id. See also* Skeel supra note 37 at 122 (noting that P&A transactions are used 54% of bank failures).

[47] *See* Ragalevasky & Ricardi *supra* note 45 at 885.

[48] See 12 U.S.C. § 1815(e)(2)(C)(ii).

[49] *Id.* at § 1815(e)(3) and § 1821(d)(6).

[50] *See* C. F. Muckenfuss III & Robert C. Eager, *Overview of the FDIC as Conservator or Receiver*, Gibson, Dunn & Crutcher LLP Publication, 6 (2008) available at http://blogs.law.harvard.edu/corpgov/files/2008/10/092608-overview-fdicasconvervator-receiver.pdf (noting that cases reviewing FDIC actions as receiver have largely upheld the FDIC's approach to the conservatorship or receivorship). *See also* Skeel supra note 37 at 123, n.8.

[51] For examples of post-seizure review, see James Madison Limited v. Ludwig, 82 F.3d 1085 (D.C. Cir. 1996); Haralson v. Federal Home Loan Bank Board, 837 F.2d 1123 (D. C. Cir. 1988); McMillian v. F.D.I.C. 81 F.3d 1041 (11th Cir. 1996); Citibank (S.D.), N.A. v. FDIC, 857 F.Supp. 976, 983 (D.D.C. 1993); DPJ Co. Ltd. v. FDIC, 30 F. 3d 247, 250 (1st Cir. 1994); Nashville Lodging Co. v. FDIC, 934 F.Supp. 449 (D.D.C. 1996); FDIC v. Parkway Executive Office Ctr., 1998 WL 18204 (E.D.Pa.).

[52] *See* Skeel supra note 37 at 139.

unwind it. This would create a messy problem of how to reverse transfers of deposits and assets that have already taken place. It is also unclear what if anything a bank would stand to gain by securing a judicial order overturning a receivership. The suit would generate publicity about the regulators' negative assessment of bank's financial condition, causing depositors to flee and potential borrowers to look elsewhere for loans. If the bank was not truly insolvent when the receivership commenced, it probably would be by the time the court set it aside. Nevertheless, even if judicial review is rarely sought, this does not mean it is meaningless. The very existence of the right to seek judicial review undoubtedly helps assure that the power to seize banks will not be abused for illegitimate ends.

The major points to note about bank receivership are, first, the process is almost entirely administrative. The FDIC runs the show from beginning to end. As noted, banks rarely mount a judicial challenge a decision to appoint the FDIC as receiver, and courts play only a minor and episodic role in reviewing the FDIC's resolution of claims once the receivership is underway. Second, the process proceeds in secret until the moment the FDIC seizes control of the bank. Bank regulators and the FDIC make no public announcement that a receivership is being contemplated and they conduct no public hearings before the seizure is announced. Bank officers and directors will know that a receivership is imminent, but it is not in their interest to disclose this. Potential bidders for bank assets are subject to confidentiality agreements and communicate with the FDIC over a secure extranet. This secrecy is justified in the name of avoiding public alarm and a run on deposits and the overriding purpose of minimizing government losses on deposit insurance.

Bankruptcy is very different. It is essentially a judicial process. Federal district courts have original and exclusive jurisdiction over all bankruptcy cases governed by Title 11 of the U.S. Code.[53] District courts routinely refer bankruptcy filings to bankruptcy judges, who are considered "Article I" judges rather than Article III judges.[54] But bankruptcy judges enjoy significant independence and resolve contested matters in the manner of courts, with adversarial public hearings featuring sworn witnesses, briefs, and written opinions. Moreover, bankruptcy courts are regarded as "adjuncts" to district courts, and district courts have the power to withdraw the reference of cases or proceedings from bankruptcy judges, in whole or in part, for good cause.[55] So-called "core" matters that arise under federal bankruptcy law can be decided

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[53] See 28 U.S.C. § 1334(a)

[54] The majority of district courts have standing reference orders in place that automatically refer all bankruptcy matters to the bankruptcy court. See 28 U.S.C. § 157(a). Should it want to intervene in any particular bankruptcy case, a district court can withdraw the reference order and take the matter away from the bankruptcy court. See 28 U.S.C. § 157(d).

[55] See 28 U.S.C. § 157(d). See generally Stern v. Marshall, 131 S.Ct. 2594, 2603-04 (2011) (summarizing the division of authority between district courts and bankruptcy courts under the bankruptcy code).

by bankruptcy judges, subject to review by district courts under an appellate review standard.[56] So-called "non-core" matters that arise under non-bankruptcy law (such as contract and tort law) are subject to de novo review by district courts.[57] Creditors are routinely given actual notice of contested matters in bankruptcy proceedings, and they will be heard, either individually or through creditor committees, before decisions materially affecting their interests are made.

In short, bankruptcy is a predominately judicial form of debt resolution. Bankruptcy judges operate much like other judges, federal district courts retain control over key decisions, and appellate review is available to challenge virtually any judgment reached. Bankruptcy is also an open process. Negotiations of course occur among different classes of creditors behind the scenes. But all affected parties are entitled to notice and to participate in formal decisions.

B. Legislative History of Dodd-Frank's OLA

The process of commencing an OLA proceeding under Title II of Dodd-Frank does not fully conform to either the banking model or the bankruptcy model. The initial draft of what became Title II was contained in the Obama Administration's proposed legislation released on July 22, 2009.[58] Title XII of this draft, entitled "Enhanced Resolution Authority," was largely drawn from existing banking legislation authorizing FDIC receiverships. In keeping with the banking model, the Administration draft provided that a receiver would be appointed administratively, in this case by the Secretary of the Treasury.[59] The draft provided for a system of elaborate administrative checks before such an appointment could be made. The Secretary had to receive the "recommendation" of the Federal Reserve Board and the Board of the FDIC by a two-thirds vote, and the Secretary had to make certain prescribed findings.[60] This was the origin of the so-called "three keys turning" required to unlock the orderly resolution process.[61]

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[56] 28 U.S.C. § 158(a).

[57] 28 U.S.C. § 157(c).

[58] Administration's Combined Draft Legislation for Financial Regulatory Reform,, Division D – Improvements for Financial Crisis Management, Title XII – Enhanced Resolution Authority ("Resolution Authority for Large, Interconnected Financial Companies Act of 2009"), 584-673 (July 22, 2009) at http://www.llsdc.org/attachments/files/252/Dodd-Frank-Act_Admn-Reg-Reform-Bill.pdf (hereafter "Administration's Combined Draft").

[59] *Id.* at § 1203(b) and § 1204(b).

[60] Administration's Combined Draft, § 1203.

[61] This 3 agency or "3-key" endorsement mechanism was previously utilized in the FDIC Improvement Act of 1991 (FDICIA). Specifically in order for the FDIC to diverge from the least cost resolution rule required under FDICIA, the Treasury must determine in consultation with the President, following a recommendation for such action by the FDIC and FED as sanctioned by a two-thirds vote of their respective boards, that such divergence is justified in order to mitigate adverse effects to the financial stability of the economy as a whole. *See* 12 U.S.C. § 1823(c)(4)(G).

The draft also followed banking law in authorizing the seized firm to file a judicial action within 30 days demanding that the receivership be set aside.[62] As under banking law, the Administration's draft language did not restrict the reviewing court in terms of the issues that it was allowed to consider in such a proceeding, nor did it put any time limit on that review. The Administration was undoubtedly aware that such a right of review is almost never exercised in the banking context. Consequently, although it would be of symbolic importance in assuring that the new resolution authority would not be abused, it would have little practical impact on the resolution process.

The House version of what became Dodd-Frank, H.R. 4173, largely tracked the Administration proposal.[63] The House bill followed the Administration draft in providing for administrative appointment of a receiver by the Secretary of the Treasury, and in prescribing the three keys turning before the Secretary could act.[64] Again following the Administration bill, the House provided for a 30-day period to seek judicial review after the receivership commenced.[65]

The Senate had somewhat different ideas. S. 3217, which was proposed by the Democratic leadership on April 15, 2010, followed the House bill in requiring three keys turning before a receiver could be appointed.[66] But it lodged the appointment authority not in the Secretary of the Treasury but in a special panel of three bankruptcy judges drawn from the Bankruptcy Court for the District of Delaware, acting on petition by the Secretary of Treasury.[67] The discretion of the bankruptcy panel was, however, tightly constrained. It could consider only a single issue before granting or denying appointment of a receiver: whether the Secretary's determination that the firm was in default or in danger of default was supported by "substantial evidence."[68]

The only explanation in the Senate Report for adding what might be regarded as a "fourth key turning" was that orderly liquidation of nonbank financial firms should be reserved for truly exceptional cases.[69] The Report stated that the threshold for triggering OLA should be "very

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[62] Administration's Combined Draft, § 1205.

[63] Wall Street Reform and Consumer Protection Act of 2010, H.R. 4173, 11th Cong., 1st Sess. §§ 1601 et seq. (2009).

[64] H.R. 4173, § 1603(a)(1).

[65] H.R. 4173, § 1605.

[66] S. 3217, U.S. Senate, 111th Cong., 2d Sess. (April 29, 2010), § 203.

[67] S. 3217, § 202.

[68] Id., § 202(b)(1)(iv).

[69] The Restoring Financial Stability Act of 2010, S. Rep. No. 111-176, 111th Cong., 2d Sess. (April 30, 2010) at 2.

high," hence, apparently, the rationale for adding "review and determination by a judicial panel,"[70] i.e., the panel of bankruptcy judges. One can speculate further about why a panel of bankruptcy judges was chosen for this role. Bankruptcy judges have expertise in recognizing when firms are in default or in danger of default, and they have a reputation for independence and objectivity. Thus, although not mentioned by the Report, the injection of the panel of bankruptcy judges into the appointment process was presumably thought to enhance the legitimacy of what was otherwise an executive branch determination to liquidate a major nonbank financial firm.

The introduction of this new threshold condition into the orderly liquidation process nevertheless posed a serious practical difficulty relative to the three keys approach advocated by the Administration and adopted in the House bill. The three keys – the Fed, the FDIC, and the Treasury – are all administrative actors, and are conditioned to act in secret, as when banking regulators and the FDIC move to declare a bank receivership. Thus, unless there is a leak, the administrative recommendations and determinations required by the three keys should not trigger a panic in financial markets or a contagion analogous to a run on the bank. Bankruptcy judges, in contrast, operate in an open fashion characteristic of traditional judicial processes. How could the substantial evidence review required of the panel of bankruptcy judges be brought into this process without jeopardizing the confidential nature of the receivership appointment process?

The answer contained in the Senate bill (although never discussed in the Senate report) was the imposition of series of extraordinary constraints on the panel of bankruptcy judges. The petition for appointment of a receiver would be filed under seal and the proceedings before the panel of bankruptcy judges held "[o]n a strictly confidential basis," with criminal penalties for disclosure.[71] Although the financial firm would be notified, creditors, counterparties, and other stakeholders would be kept in the dark. The panel would have to rule very quickly – within 24 hours of the filing of the petition.[72] The Senate bill did not address what happened if the panel failed to make their decision within the requisite 24 hour time period.[73] Once the petition was granted, there could be no stays pending appeal to the courts.[74]

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[70] Id.

[71] S. 3217, supra, §§ 202(b)(1)(A)(iii); 202(b)(1)(C).

[72] Id., § 202(b)(1)(iii). ("On a strictly confidential basis, and without any prior public disclosure, the Panel, after notice to the covered financial company and a hearing in which the covered financial company may oppose the petition, shall determine, within 24 hours of receipt of the petition filed by the Secretary, whether the determination of the Secretary that the covered financial company is in default or in danger of default is supported by substantial evidence.")

[73] Id., § 202(b)(1)(iv)(I)&(II).

[74] Id. § 202(b)(1)(B).

These provisions are jarring if we think of the panel of bankruptcy judges as a court. But the constitutional issues they present are diminished given the status of bankruptcy judges as "Article I" judges. For constitutional purposes, bankruptcy judges are little different than Administrative Law Judges in the Executive Branch.[75] Thus, the role of the panel of bankruptcy judges under the Senate bill was not significantly different from a hypothetical provision requiring a panel of ALJs in the Treasury Department to determine that there is substantial evidence a firm is in default or danger of default.[76] Moreover, the provisions precluding any stay of the panel's order pending appeal are not terribly different from the judicial review provisions under the banking law, which provide for judicial review only after a receivership has commenced.[77] Allowing an appeal without a stay is functionally similar to allowing an appeal only after a receivership has commenced.

There was, however, one important difference in the Senate bill's judicial review provisions. Under the Administration proposal and the House bill, there was no limitation on the legal or factual issues that could be presented to the court in challenging the appointment of a receiver after the receiver was appointed. Under the Senate bill, any appeal to the courts from the determination of the bankruptcy panel was to be limited to whether the Secretary's determination that the firm was in default or in danger of default was supported by substantial evidence. This is a far more restricted right of judicial review than that provided by the bank receivership laws, which put no limit on the issues a reviewing court can consider and appear to contemplate that the review will be de novo as to both fact and law. Of course, as we have seen, the right of judicial review is virtually never exercised in the bank receivership context. Still, a right of judicial review is an important safeguard, and limiting review to a single factual question under a deferential standard of review is a much weaker form of protection against executive abuse than that provided by the banking laws.

Less than a month after the Senate bill was released, Senator Dodd proposed "for himself and Mr. Shelby" – the senior Republican on the Senate Finance Committee who had filed a dissenting report to the Senate bill -- a series of amendments to the Senate bill.[78] The first of

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[75] See Northern Pipeline Construction Company v. Marathon Pipeline Company, 458 U.S. 50, 60-61 (1982) ("It is undisputed that the bankruptcy judges... do not enjoy the protections constitutionally afforded to Art. III judges. The bankruptcy judges do not serve for life subject to their continued 'good Behaviour., Rather, they are appointed for 14-year terms, and can be removed by the judicial council of the circuit in which they serve on grounds of 'incompetency, misconduct, neglect of duty, or physical or mental disability.' Second, the salaries of the bankruptcy judges are not immune from diminution by Congress... In short, there is no doubt that the bankruptcy judges created by the Act are not Art. III judges.")

[76] Such a provision, if not subject to review by the Secretary of the Treasury, might nevertheless give rise to objections under Article II.

[77] 18 U.S.C §1821(c)(7).

[78] Congressional Record 111th Cong., SA 3739 (May 5, 2010).

these amendments made a further critical change in the method of appointing a receiver to commence the orderly liquidation process. Rather than have a panel of bankruptcy judges appoint a receiver on petition by the Secretary of the Treasury, the amendment provided that the receiver was to be appointed by the United States District Court for the District of Columbia. Now, for the first time, the receiver was to be formally appointed by an Article III judge, not an executive branch agency or a panel of "Article I" judges. The modified Senate bill also changed the standard of review to be applied by the District Court from "substantial evidence" to "arbitrary and capricious," and added that the court was to consider whether the firm was a "financial firm" as well as whether it was in default or in danger of default.[79] No explanation was offered for the change. The amendment was adopted and incorporated into the final Senate version of the legislation, described as a substitute version of H.R. 4173.[80] This revised bill was approved by the Senate on May 27, 2010.[81]

The public record is silent as to who proposed that the receiver be appointed by an Article III judge or why they thought this was important. Circumstantial evidence suggests at least one Senator must have insisted on this unusual form of "ex ante review" as a condition of his or her vote. Senator Dodd, the Chairman of the Senate Finance Committee and the floor manager of the legislation in the Senate, needed sixty votes to avoid a filibuster.[82] In order to get to sixty, he had to count on several shaky Democratic votes plus at least two Republicans, including the newly-elected Senator from Massachusetts, Scott Brown.[83] When the divergent House and Senate bills went to the Conference Committee, the House conferees listed as one of the changes it wanted the elimination of the Senate's recently adopted provision for ex ante judicial review.[84] The Senate refused, without explanation.[85] The House then insisted on the change,[86] but the

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[79] Senate Substitute, § 202(a)(1)(A)(iii).

[80] Restoring American Financial Stability Act of 2010, Senate Substitute for H.R. 4173, 111th Cong. , 2nd Sess. (May 20, 2010).

[81] Congressional Record 111th Congress, S4560 (May 27, 2010).

[82] ROBERT KAISER, A CONGRESSIONAL ACT, (Alfred A. Knopf, ed. 2013)

[83] See Jia Lynn Yang, *Scott Brown's Key Vote Gives Massachusetts Firms Clout In Financial Overhaul*, WASH. POST (June 23, 2010).

[84] Wall Street Reform & Consumer Protection Act, conferee deliberations, Title II, House Proposed Offer to Title II (sent to Senate June 17, 2010) at http://democrats.financialservices.house.gov/FinancialSvcsDemMedia/file/key_issues/Financial_Regulatory_Reform/TITLEII_OFFER.pdf

[85] Wall Street Reform & Consumer Protection Act, conferee deliberations, Senate Counter Offer: Title II, Orderly Liquidation Authority (sent to House on June 17, 2010) at http://democrats.financialservices.house.gov/singlepages.aspx?NewsID=3&RBID=775.

Senate again refused to relent.[87] The House at that point capitulated. A plausible inference is that the Senate conferees could not have caved in on the provision for appointment authority without endangering the razor-thin margin needed for sixty votes to approve the legislation once it emerged from the Conference Committee. Accordingly, the Senate version, calling for appointment of the FDIC as receiver by an Article III court, was approved by the Conference Committee, adopted by both the House and Senate, and signed by the President.[88]

C. OLA As Enacted

The relevant provisions of Title II, as enacted, can be briefly summarized.

The internal administrative process that precedes the petition to the District Court for the District of Columbia for appointment of a receiver is described by the statute as a "systemic risk determination."[89] The Treasury must undertake an analysis to establish that the triggering conditions warranting orderly liquidation have been met. Specifically, the statute requires the Secretary to make seven affirmative findings before making a determination to seek a receivership:

1. The financial company must be in default or in danger of default.
2. The company satisfies the definition of a financial company.
3. The failure of the financial company would have serious adverse effects on financial stability in the United States.
4. No viable private sector alternative is available to prevent default.

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[86] Wall Street Reform & Consumer Protection Act, conferee deliberations, House Counter Offer: Title II, Orderly Liquidation Authority (sent to Senate on June 23, 2010) at http://democrats.financialservices.house.gov/FinancialSvcsDemMedia/file/key_issues/Financial_Regulatory_Reform/Conference_on_HR_4137/Title_II/Title_II_House_Counteroffer_6_23_2010.pdf.

[87] Wall Street Reform & Consumer Protection Act, conferee deliberations, Senate Counter-Counter Offer: Title II, Orderly Liquidation Authority (sent to House June 24, 2010) at http://democrats.financialservices.house.gov/FinancialSvcsDemMedia/file/key_issues/Financial_Regulatory_Reform/Conference_on_HR_4137/Title_II/Senate_Title_II_Counteroffer_Revised_6_24.pdf.

[88] See Wall Street Reform and Consumer Protection Act – Conference Report (July 15, 2010) at http://thomas.loc.gov/cgi-bin/query/C?r111:./temp/~r111AUEIkn; See also Administration of Barack H. Obama, 2010, *Remarks on Signing the Dodd-Frank Wall Street Reform and Consumer Protection Act* (July 21, 2010) at http://www.gpo.gov/fdsys/pkg/DCPD-201000617/pdf/DCPD-201000617.pdf.

[89] DFA, § 203.

5. Any effect of a receivership on creditors, counterparties, and shareholders would be "appropriate" given the benefits of a receivership in terms of preserving financial stability.

6. Establishing a receivership would avoid or mitigate the adverse effects on stakeholders relative to not undertaking such action.

7. The company has been ordered by regulators to convert all if its convertible debt instruments.[90]

The statute also adopts the three keys turning that initially appeared in the Administration's draft legislation. The Secretary must obtain the written recommendation by a two-thirds vote of the members of both the Federal Reserve Board and the FDIC before a petition is authorized.[91] The statute further provides that the Secretary must consult with the President before filing a petition.[92]

There is no indication in the statute that the covered firm has any right to participate in this administrative process. Conceivably the Treasury could provide by regulation for notice and an opportunity to be heard by affected private interests before any petition for appointment of a receiver is made, which would mitigate what otherwise would appear to be a deficiency of due process.[93] But the statute does not require this, the assumption of the need for secrecy would seem to preclude this, and there is no sign that such regulations are contemplated. The statute does state that the Secretary shall "notify the covered financial company" when he makes a determination to file a petition,[94] and there could be a gap between the Secretary's notification of the "determination" and the filing of the petition in court, which would give the financial company time to prepare for the court proceedings. But again, the statute does not require that the notification of the determination occur before the filing of the petition, and the concern for

[90] DFA, § 203(b).

[91] Different bodies must provide written recommendations if the covered financial firm is a broker/dealer or an insurance company.

[92] DFA, § 203(b).

[93] To date, the Treasury Department has not promulgated any regulations regarding how notice of its receivership determination must be provided to the failing financial company much less whether such notice must also be provided to affiliated parties with significant interests at stake. While the possibility of some future regulation along these lines is not out of the question, given the Treasury's objection to the 48 hour advance notice requirement for any receivership petition to the DC District Court (a requirement contained in the originally issued Local Civil Rule 85), any rule regarding the provision of advance noticed to anyone implicated by the Treasury's receivership decision certainly seems unlikely. See Bankruptcy: Agencies Continue Rulemakings for Clarifying Specific Provisions of Orderly Liquidation Authority, United States Government Accountability Office, Report to Congressional Committees (GAO-12-735), 15-16 (July 2012).

[94] DFA, § 202(a)(1)(A)(i).

swift and secret action would work against giving the covered firm any realistic period of time to prepare to do battle in court.

Once the executive branch decides that a financial firm should be placed in receivership, it files a petition for appointment of a receiver under seal with the District Court for the District of Columbia. The statute provides for stiff criminal penalties for anyone who "recklessly" discloses the determination to file a petition, the content of petition, or "the pendency of the court proceedings."[95] Creditors and other stakeholders receive no notice and, given the criminal prohibition on disclosure, have no way of intervening to defend their interests. If the court does not rule on the petition within 24 hours, it is automatically granted.[96] In effect, the statute contemplates that a covered financial firm will be notified that the Treasury wants it liquidated and it is given the balance of 24 hours to review the Treasury petition and findings, prepare a rebuttal and file it with the court, and convince the court after a hastily convened hearing to reject the petition.[97]

The statute also severely limits the court in terms of what issues it can consider. The court is permitted to consider only the Secretary's determination that the firm is a "financial company" as defined by the Act, and his determination that the firm is "in default or in danger of default."[98] Moreover, the court is limited to considering whether these two determinations are "arbitrary and capricious."[99] The statute provides that if the District Court finds one or both of the Secretary's determinations to be arbitrary and capricious, the court must remand to the Secretary and afford the Secretary "an immediate opportunity to amend and refile the petition."[100] No other relief is mentioned; evidently the Secretary can keep refilling until the District Court grants the petition. An appeal is allowed within 30 days to the D.C. Circuit, and a petition for certiorari is allowed to the Supreme Court within 30 days of a ruling by the D.C. Circuit.[101] But no stay is allowed pending appeal, so the receivership goes forward once the petition is granted, even if the firm files an appeal. The statute again limits the issues that can be

[95] DFA, § 202(a)(C) (carrying a maximum penalty of 5 years imprisonment and a $250,000 fine).

[96] DFA, § 202(a)(1)(A)(v).

[97] The statute directs the District Court for the District of Columbia to adopt rules implementing the provisions for appointment of a receiver. DFA, § 202(b). Those rules were adopted on July 6, 2011. See Local Civil Rule 85, United States District Court for the District of Columbia *as amended on July 6, 2011* (January 19, 2011) at http://www.dcd.uscourts.gov/dcd/sites/ dcd/files/2011_LCvR_85_Dodd-Frank_Amended.pdf (hereafter "Local Civil Rule 85"). For further discussion, see TAN infra.

[98] DFA, § 202(a)(1)(A)(iii).

[99] DFA, § 202(a)(1)(A)(iv)(I)&(II)).

[100] DFA, § 202(a)(1)A)(iv).

[101] DFA, § 202(a)(2)A)(i) & DFA, § 202(a)(2)(B)(i).

considered by the court of appeals or the Supreme Court: they may only inquire whether the findings that the firm is a covered financial firm and is in default or in danger of default are "arbitrary and capricious."[102] The language of the statute is more emphatic in limiting the issues that may be considered on appeal, stating that review "shall be limited" to these two issues.[103]

Once the court grants the petition appointing the FDIC as receiver of the covered financial firm, the process moves out into the open. The statute describes in excruciating detail a special kind of receivership which in some respects resembles an FDIC receivership of a bank, and in other respects resembles ordinary bankruptcy, with the FDIC exercising most of the powers of a debtor in possession or trustee in bankruptcy.[104] Upon being appointed, the FDIC as receiver exercises all the powers of the financial firm, including the power to operate the company, hire and fire employees, and retain the services of third-party service providers.[105] But the FDIC also acts like a bankruptcy court. It can order a stay of further proceedings to collect debts against the covered financial firm,[106] can unwind fraudulent and preferential transactions,[107] can bring actions to collect monies owed to the firm,[108] and considers and resolves claims of various classes of creditors against the firm.[109] If any creditor is dissatisfied with the FDIC's resolution of a claim, it can bring a judicial action in the United States District Court where the covered financial firm has its principal place of business, and the court will rule on the claim.[110] There is, however, no requirement of court approval of other significant actions by the FDIC, such as the creation of a bridge financial company, the sale of assets, or the final liquidation of the covered firm.

II. Constitutional Challenges: The Who and the When

A variety of potential constitutional challenges could be made to Title II's statutory scheme. The secret, 24-hour proceeding in which the FDIC is appointed receiver by the District

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[102] DFA, § 202(a)(2)(B)(iv).

[103] DFA, §§ 202(a)(2)(A)(iv); 202(a)(2)(B)(iv).

[104] See generally Douglas G. Baird and Edward R. Morrison, Dodd-Frank for Bankruptcy Lawyers, 19Am. Bankr. Inst. L. Rev. 287 (Winter 2011).

[105] DFA, § 210(a)(1)(A).

[106] DFA, § 210(a)(8).

[107] DFA, § 210(a)(11)(A)&(B).

[108] DFA, § 210(a)(1)(B)(ii).

[109] DFA, § 209 and § 210(a)(2).

[110] DFA, § 210(a)(4).

Court of the District of Columbia can be challenged as violating due process or Article III. The scheme can also be challenged as violating the "uniformity" requirement of the Bankruptcy Clause or the First Amendment. Constitutional challenges under the Takings Clause can also be imagined, depending on how particular issues are resolved during the receivership. But first we must consider who can bring these sorts of constitutional claims and when they might be advanced.

We will discuss three possibilities: (1) raising constitutional claims defensively in the proceeding brought by the Secretary of the Treasury to appoint a receiver; (2) filing an independent action under 28 U.S.C. § 1331 to enjoin the receivership once it is approved (but before it has taken significant steps to unwind the firm); and (3) filing an action to enjoin the appointment of a receiver before the Secretary files a petition to appoint a receiver. This last option is essentially the one being pursued in the complaint recently filed by the state attorneys general.[111]

Ordinarily, raising constitutional claims defensively would be the least problematic course of action. If the government files a legal action in which it demands the defendant's person or property, there is no doubt the defendant can raise any constitutional objections she may have by way of defense.[112] Standing is clearly established: concrete injury has either occurred or is "certainly impending."[113] Jurisdiction is based on the authority invoked by the government in bringing its action.[114] There is no need to demonstrate a cause of action, since the defendant is raising the Constitution by way of defense. The government might try to argue that raising constitutional defenses is here impliedly precluded by statute. Specifically, by limiting review to whether the two determinations are arbitrary and capricious, the statute impliedly precludes consideration of other issues. Given the established canon that implied preclusion of review of constitutional questions is not favored, however, it is difficult to see how this would succeed. It is well established that Congress must speak with clarity before it cuts off constitutional claims, and the Court has said a "grave constitutional question" would be presented if such a clear statement of preclusion were ever encountered.[115] Nothing in Title II

[111] See *Big Spring Second Amended Complaint* supra note 29.

[112] Henry M. Hart, The Power of Congress to Limit the Jurisdiction of Federal Courts: An Exercise in Dialectic, 66 Harv. L. Rev. 1362 (1953).

[113] Clapper v. Amnesty International USA, No. 11-1025 (February 26, 2013), slip op. at 15.

[114] See 28 U.S.C. § 1345.

[115] Johnson v. Robison, 415 U.S. 361 (1974); Webster v. Doe, 486 U.S. 592, 619 (1988).

comes close to a clear statement precluding constitutional defenses.[116] Thus, if and when the Secretary of the Treasury files a petition with the District Court for the District of Columbia asking for the appointment of a receiver to liquidate a financial firm, the firm (and possibly its officers or directors) can interpose constitutional defenses in response to the petition.

The peculiar procedures set forth in Title II greatly complicate this conventional approach. One problem is notice. Some stakeholders will know about the Secretary's petition, namely, the directors and principal officers of the firm targeted for receivership and liquidation. But other stakeholders – including creditors, counterparties, most employees of the firm, and the shareholders of the firm – cannot raise constitutional objections defensively, because Dodd-Frank makes no provision for giving them notice, requires that the court proceedings be conducted "on a strictly confidential basis,"[117] and indeed makes it a criminal offense for anyone who is aware of the proceeding to give any third party notice.[118] If there is no legal way to obtain notice of adverse action by the government, one cannot defend against it, on constitutional or any other grounds. Equally problematic, the district court cannot conceivably give adequate consideration to any constitutional defense in 24 hours. The government will insist that the statute requires adhering to the 24 hour deadline, at which point the petition is deemed automatically granted and no stay is possible. Further, the government would likely claim, action is urgently needed to avert a financial crisis. Faced with a conflict between a strict statutory deadline and government warnings of financial crisis, on the one hand, and its duty to enforce the Constitution, on the other, what is the court going to do?

Conceivably, the court could try to solve the problem by invoking the Constitution as authority to make modest modifications in the statutory procedures. For example, the court could grant a temporary stay of further action on the petition in order to afford an adequate period of time to brief and consider the constitutional issues presented. Remember, at this point the proceedings are confidential and the papers have been filed under seal.[119] If the court is persuaded that the constitutional defenses are serious, it might be willing to grant a short stay, perhaps of a few days, in order to give the issues fuller consideration. If after this period of expedited consideration the court concludes that the statute is unconstitutional in one or more respects, it could order more permanent injunctive relief that would cure the constitutional defect

[116] Other provisions of the Act address questions of judicial review, but they cut off judicial proceedings asserting claims against the firm while it is in receivership – except those specifically allowed -- or actions against the FDIC in its capacity as receiver – again unless expressly allowed. DFA, 210(a)(9)(D); DFA, 210(e).
These provisions do not address review of the Secretary's decision to seek to have a receiver appointed, nor do they address possible constitutional challenges to the Act or any of its provisions.

[117] DFA § 202(a)(1)(A)(iii).

[118] DFA § 202(a)(1)(C).

[119] DFA § 202(a)(1)(A)(ii).

and allow the petition to be considered in a manner consistent with constitutional requirements.[120] This constitutional ruling would, of course, be subject to appeal by the government (including a request for a stay or emergency relief) under the ordinary rules of appellate procedure. This solution is problematic, however, because it requires the court effectively to re-write statute before deciding whether it is constitutional. Also, it also does nothing to provide notice to other stakeholders who may want to raise constitutional objections.

A second approach might be for any stakeholder who is aggrieved by the appointment of a receiver and pending liquidation of the firm to file an independent action in the district court seeking to enjoin the receivership on constitutional grounds. Jurisdiction would be based on 28 U.S.C. § 1331, which applies to actions grounded in the Constitution. Standing would be established by the prospective liquidation of the firm or loss of rights or claims having monetary value. The cause of action could be based on the Administrative Procedure Act (APA), which provides that "[a]gency action made reviewable by statute and final agency action for which there is *no other adequate remedy in a court* are subject to judicial review."[121] The Secretary's decision to petition for a receivership would be final agency action, and Dodd-Frank's draconian 24 hour time limit and requirement that judicial proceedings remain in camera would preclude that statute from affording "an adequate remedy in court." This approach also has the virtue that it would be filed immediately after the receivership is established, and so the automatic stay powers given to the receiver would be in effect, providing a temporary stabilization of the situation and hopefully forestalling financial panic and behavior analogous to a run on the bank.

Unfortunately, Dodd-Frank appears to eliminate this option, at least for some constitutional claims. It says:

> Except as provided in this title, no court may take any action to restrain or affect the exercise of powers or functions of the receiver hereunder, and any remedy against the Corporation or receiver shall be limited to money damages determined in accordance with this title.[122]

This would seem to preclude any action to "restrain or affect" the receiver based on constitutional claims in an action brought under 28 U.S.C. § 1331. Thus, for example, no court could entertain an action to enjoin the receiver on the ground that the statute violates the uniformity requirement of the Bankruptcy Power or the Takings Clause. This preclusion of review, however, might not affect constitutional claims addressed to the initial proceeding in the

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[120] An issue of severability would be presented, at least implicitly. But it seems unlikely that the entire Dodd Frank Act should fall on constitutional grounds because of one or more constitutional infirmities in the process for appointing a receiver.

[121] APA, 5 U.S.C. § 704.

[122] DFA, § 210(e).

district court to *appoint* a receiver, including those based on due process, Article III, or the First Amendment. These claims challenge the judicial process to appoint the receiver, and so do not seek to "restrain or affect" the powers of the receiver once appointed. As to defects in the appointment process, a bit of litigational jujitsu might be possible by filing a motion under Rule 60(b) to set aside the final judgment approving the receiver, on the ground that the judgment was obtained under procedures that violate the Constitution.[123] The Rule 60(b) motion would not be governed by the time limits or the gag order of Dodd-Frank,[124] and hence would not encounter the problems that seem to doom any constitutional defense raised in response to petition itself. Still, even if this works for claims directed to the judicial process for appointing a receiver, it would not work for other constitutional objections to Title II.

The third option would be to file an action challenging the constitutionality of the Act before the Secretary files a petition to appoint a receiver. Here, standing would likely be the most serious problem, particularly if the firm or one of its stakeholders bringing the action cannot demonstrate that action by the government is threatened or "certainly impending."[125] It would be necessary to show that the government is seriously contemplating using its OLA to appoint a receiver, but that will be difficult if the government is successful in keeping its internal deliberations secret.

Do the state attorneys general stand on firmer footing in being able to mount a challenge to Title II before it has been applied to any individual firm? Arguably they do. Although the Court has rejected the States' standing to challenge the constitutionality of federal legislation on behalf of their citizens through parens patriae suits,[126] recent decisions suggest growing liberality toward state standing. In *Massachusetts v. EPA*, where the State sought to challenge the government's failure to regulate global warming, the Court spoke mysteriously about States enjoying "special solicitude" relative to private parties in determining standing to sue.[127] More recently, in the Affordable Care Act litigation, serious questions were raised about the States' standing, with the Fourth Circuit ruling that Virginia lacked standing to challenge the individual mandate.[128] The Supreme Court declined to review this ruling, and went on to consider a wide-

[123] See FRCP Rule 60.

[124] *Id.* at 60(c)(1) ("A motion under Rule 60(b) must be made within a reasonable time--and for reasons [set forth at 60(b)](1), (2), and (3) no more than a year after the entry of the judgment or order or the date of the proceeding.")

[125] Clapper v. Amnesty International USA, No. 11-1025 (February 26, 2013), slip op. at 15; Lujan v. Defenders of Wildlife, 504 U.S. 555, 562 (1992).

[126] Massachusetts v. Mellon, 262 U.S. 447 (1923).

[127] 549 U.S. 497, 505 (2007).

[128] Virginia ex el. Cuccinelli v. Sebelius, 656 F.3d 253 (4th Cir. 2011).

ranging challenge to the individual mandate brought by 26 States among others, without uttering a word about standing.[129] This, of course, does not mean the Court found that the states had standing. There were other plaintiffs in the case, including individuals, and the Court may have implicitly concluded they had standing to challenge the mandate. At least in terms of optics, however, the Affordable Care Act litigation lends further support to the idea that state standing is to be quite liberally construed.

The attorney general lawsuit that challenges the constitutionality of Title II of Dodd-Frank rests on the states' interest in their employee pension funds, which include investments in firms that are potentially eligible for liquidation under Title II. Although none of these firms is currently threated with orderly resolution under Dodd-Frank, the states argue that the statute has taken away their federal statutory right to have their interests as creditors treated the same as other similarly-situated creditors.[130] They argue that this abrogation of rights is a present invasion of a legally protected interest, and hence satisfies the Article III requirement of actual immediate injury.[131] The statutory right to equal treatment of creditors, however, is one that will come into play only when a debtor is in default or in danger of default. If the mere existence of a debt were enough to confer standing to challenge a change in the legal treatment of creditors, it would seem that any person should be able to challenge any change in the law that might conceivably affect their interests as creditors sometime in the future. This is clearly not the law.[132] Also an injury caused by Dodd-Frank's authorization of departures from equal treatment of similarly-situated creditors bears no causal relationship to the due process, Article III, and First Amendment objections to the statute.[133] Thus, it is not clear that this alleged injury, even if otherwise sufficient to confer standing, would support standing to challenge the constitutionality of OLA. So we are doubtful that the D.C. Circuit will uphold the states standing to challenge Title II, in the absence of some evidence that OLA is about to be invoked in a way that would affect their financial interests.

Finding a cause of action could also become an issue. The APA, to repeat, provides that "[a]gency action made reviewable by statute and *final agency action* for which there is no other adequate remedy in a court are subject to judicial review."[134] If the Secretary has not made a

[129] National Federal of Independent Business v. Sebelius, 132 S.Ct. 2566 (2012).

[130] State Plaintiffs' Memorandum in Opposition to Defendants' Motion to Dismiss the Second Amended complaint, State National Bank of Big Spring v. Wolin, No. 1:12-cv-0132 (ESH) (filed Feb. 27, 2013) at 16-19.

[131] Id. at 19-24.

[132] Summers v. Earth Island Inst., 555 U.S. 488, 496 (2009); Defenders of Wildlife, 504 U.S. at 572-73.

[133] It is not clear that it even implicates the uniformity requirement of the Bankrutpcy Clause, if that clause is interpreted to require that debtors be treated uniformly, as opposed to creditors. See discussion infra.

[134] APA, 5 U.S.C. § 704.

determination to file a petition, it would be difficult to claim that there is *final* agency action to review. Absent a cause of action under the APA, the cause of action would have to be implied directly from the Constitution, as in *Bivens* and following cases.[135] The Court has been cutting back on these implied rights based on the Constitution. Most relevantly, the Court in *FDIC v. Meyer*[136] held that there is no implied *Bivens* action against a federal administrative agency (the FDIC as it happens) as opposed to individual federal officers. This still leaves open the possibility of an *Ex Parte Young*-style action seeking to enjoin federal officers, such as the Secretary of the Treasury, for threatening to take action alleged to violate the Constitution. There is a debate of sorts, at least in academic circles, about whether an implied right of action can be said to exist even in these circumstances.[137] As things currently stand, however, the *Ex Parte Young* cause of action is good law, and we assume the lower federal courts will continue to treat it as such unless or until the Supreme Court says otherwise. So on this slender reed, there should be an available cause of action for anticipatory relief.

If the standing obstacle can be overcome, this might be the best of the three options. The action would not be subject to the time limits or the notice prohibitions of Dodd-Frank, which only come into play after the petition is filed. And it would not be limited by the preclusion of actions that seek to "restrain or affect" the powers of the receiver, because the receiver would not have been appointed.

Whichever option is chosen, the government would undoubtedly seek to defeat any request for injunctive or declaratory relief on the ground that the firm and its stakeholders will suffer no irreparable injury if the constitutional arguments are postponed until after the OLA process is complete. The doctrinal vehicle for advancing this argument might be the Tucker Act,[138] and the established proposition that takings claims can be postponed until after the government action is complete, provided all the interests at stake can be fully protected by a suit for damages in the Court of Federal Claims under the Tucker Act. Relevant Supreme Court authority, perhaps most notably the *Regional Rail Reorganization Act Cases*,[139] holds that Congress will not be presumed to cut off a Tucker Act remedy absent a clear statement to the contrary. Dodd-Frank contains language that cuts off any remedy against the *FDIC as receiver*

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[135] Bivens v. Six Unknown Fed. Narcotics Agents, 403 U.S. 388 (1971).

[136] 510 U.S. 471 (1994).

[137] See, e.g., John Harrison, Ex Parte Young, 60 Stan. L. Rev. 989 (2008); Ann Woolhandler, The Common Law Origins of Constitutionally Compelled Remedies, 107 Yale L. J. 77 (1997).

[138] 28 U.S.C. § 1491.

[139] Blanchette v. Connecticut General Ins. Corporations, 419 U.S. 102, 126-127 (1974); see also Ruckelshaus v. Monsanto Co., 467 U.S. 986, 1018-1019 (1984); Preseault v. I.C.C., 494 U.S. 1, 13 (1990).

except an action for money damages as authorized by Title II.[140] But the Tucker Act authorizes suits against *the United States* for takings or breach of contract. So perhaps the Tucker Act remedy has not been clearly foreclosed by Dodd-Frank.

The government would likely seek to bolster its no irreparable harm argument by claiming that all the interests at stake are in the nature of fungible financial assets – dollars – and that such interests by their very nature can be vindicated by ex post monetary awards, with interest to reflect the time value of money. Creditors who claim their security interests have been violated, officers who claim their salaries have been wrongfully clawed back, directors deprived of their paid positions – all these aggrieved persons can be made whole by an award of money damages. Unlawful action that can be rectified by a payment of money damages is generally regarded as not presenting the kind of irreparable harm that justifies mandatory relief.[141]

If the only constitutional questions presented were takings claims and impairment of contract claims, and the government's authority were otherwise uncontested, then this argument would be well founded. But if the government's authority to proceed in the manner directed by the statute is challenged on other constitutional grounds, then an ex post award of money damages is not sufficient to vindicate the claim.[142] The Due Process Clause says that no one shall be deprived of property without due process of law. This generally means, at least when conventional property interests are at stake, that a person must be given an opportunity to challenge the legal authority of the government before their property is taken.[143] Thus, if a firm makes a credible contention that government is seeking to have it liquidated in a manner contrary to law, this issue should be resolved before rather than after the government liquidates the firm.

[140] DFA, 210(e) ("[A]ny remedy against the corporation or receiver shall be limited to money damages determined in accordance with this title.") See also DFA 210(a)(8)(D) ("Except as otherwise provided in this title, no court shall have jurisdiction over…any claim relating to any act or omission of …the Corporation as receiver."). By and large any claims against the FDIC will involve creditors and others with various rights stemming from their pre-receivership relationship with covered financial company that were extinguished or modified when the company was placed into FDIC receivership pursuant to the OLA.

[141] See Weinberger v. Romero—Barcelo, 456 U.S. 305, 311–313 (1982); Amoco Production Co. v. Gambell, 480 U.S. 531, 542 (1987); eBay Inc. v. MercExchange, L.L.C., 547 U.S. 388, 391 (2006) ("According to well-established principles of equity, a plaintiff seeking a permanent injunction… must demonstrate [,among other things,]… that remedies available at law, such as monetary damages, are inadequate to compensate for that injury…").

[142] Even takings claims are subject to this limiting principle. The Takings Clause has been read to mean that the government can take property only for a public use. Kelo v. City of New London, 545 U.S. 469 (2005). If a property owner contends the taking is not for a public use, then this issue must be resolved before the taking occurs, not afterwards. If the issue is postponed, and the taking is later determined not to be for a public use, then there will be no way to correct the constitutional violation. An award of just compensation cannot remedy a constitutional right that property not be taken, period. We are not suggesting a firm could mount a successful public use argument against a Dodd Frank receivership. The point is more general.

[143] E.g., Connecticut v. Doehr, 501 U.S. 1 (1990).

Once the firm's assets are sold, and it is liquidated, it cannot be put back together again. Claims based on Article III of Constitution, the uniformity requirement of the Bankruptcy Clause, or the First Amendment would also seem to be the sorts of claims that cannot be rectified by ex post awards of damages. At least as to these sorts of constitutional claims, the firm the government wants to liquidate will suffer irreparable harm if the inquiry is postponed until after the liquidation is over.

III. Constitutional Issues – Process Objections

The prospect of appointment of the FDIC to liquidate a firm under Title II would likely trigger deep anxiety by a variety of stakeholders of the targeted firm. Creditors would worry that they will not get their money back, even if it is secured by collateral. Holders of derivatives or swaps would worry that their contracts will be modified or repudiated. Officers and directors would worry that they will be out of a job. Shareholders would be distraught at the prospect of having their investment wiped out. Each of these groups would have an incentive to bolster their position by raising constitutional objections to the OLA process. Arguments conceivably could be advanced under Due Process Clause of the Fifth Amendment, under Article III of the Constitution, under the Uniformity Clause of the Bankruptcy Power, under the First Amendment, and under the Takings Clause of the Fifth Amendment. We consider in this Part process objections that would be brought in the name of due process and Article III.

A. Due Process

In order to establish a violation of due process, a claimant must show that he has an interest in life, liberty or property, that the government is threatening to deprive him of this interest, and that the deprivation will take place without providing the notice or opportunity to be heard required by due process of law.

We assume that all the relevant parties who might feel threatened by the prospect of liquidation of a firm under Title II would satisfy the threshold requirement of having a "property" interest at stake. Due process property includes money and securities. Thus, creditors of all stripes have property for due process purposes in the assets of a debtor firm.[144] Property also includes a paying job, at least if one has an unexpired employment contract that makes one more than an employee at will.[145] Consequently, officers and directors who will lose

[144] See Tulsa Professional Collection Services, Inc. v. Pope, 485 U.S. 478, 485 (1988) (holding that unsecured creditor's claim is "property" for purposes of procedural due process).

[145] Federal Deposit Insurance Corp. v. Mallen, 486 U.S. 230, 240 (1988) ("[A]ppellee's interest in the right to continue to serve as president of the bank and to participate in the conduct of its affairs is a property right protected by the Fifth Amendment Due Process Clause"); Cleveland Bd. Of Education v. Loudermill, 470 U.S. 532, 538-41 (1985).

their positions through an exercise of OLA have due process property, provided they are working under an unexpired employment contract. It is also undeniable that the actions taken by the FDIC in completing an orderly liquidation constitute state action that would deprive these parties of their respective interests.

In assessing what process is due, the Court has tended to treat notice as a requirement distinct from other procedural elements.[146] Actual notice by mail or the equivalent is generally required for any proceeding that will adversely affect the property rights of an affected party, as long as their name and address are "reasonably ascertainable."[147] This would seem to call into question the feature of the statute that makes it a criminal offense to provide notice to anyone other than the firm to be placed into receivership.[148] Shareholders, counterparties, creditors, and officers deemed to be responsible for the financial distress of the firm may have their interests compromised or completely wiped out by the mandatory liquidation of Title II, and yet the statute makes it a crime to provide them with notice that would allow them to voice their objections before that process commences.

The government would undoubtedly point to bank receiverships, where by tradition no formal notice is given before a receiver is appointed and seizes the property. In practice, the appointment of a receiver will typically come as no surprise to the bank and its officers and directors.[149] As the D.C. Circuit has observed, bank regulators ordinarily will have raised concerns about the adequacy of the bank's reserves or other financial issues with bank officers over an extended period of time, giving the bank a clear idea of the relevant issues and an opportunity to respond, however informally.[150] Whether nonbank financial firms will similarly be alerted to the possibility of seizure under Title II through informal communications with regulators is unclear; certainly the statute does not require it. And even if the firm has been given effective notice, this does not mean notice will be given to creditors and other stakeholders, to whom notice is prohibited.

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[146] Jones v. Flowers, 547 US 220, 223 (2006) ("Before a State may take property… the Due Process Clause of the Fourteenth Amendment requires the government to provide the owner notice and opportunity for hearing appropriate to the nature of the case.") (internal punctuation and citations omitted); see also Fuentes v. Shevin, 407 U.S. 67, 80 (1972) ("For more than a century the central meaning of procedural due process has been clear: Parties whose rights are to be affected are entitled to be heard; and in order that they may enjoy that right they must first be notified.") (internal punctuation and citations omitted),

[147] Mennonite Board of Missions v. Adams, 462 U.S. 791, 800 (1983); Mullane v. Central Hanover Brank & Trust Co., 339 U.S. 306, 314 (1950).

[148] DFA, § 202(a)(1)(C).

[149] But see David Zaring, A Lack of Resolution, 60 Emory L. J. 97, 119 (2010) (noting that in 2009 twenty-one banks were closed "without any prior notice by the agency.").

[150] James Madison Limited v. Ludwig, 82 F.3d 1085, 1099-1101 (D. C. Cir. 1996).

The government will inevitably be thrown back on the position that sometimes exigent circumstances require that the government act without giving advance notice, as in a public health emergency. The government will argue that advance notice to all reasonably ascertainable stakeholders cannot be given before a seizure of the firm pursuant to OLA, because this could trigger the very financial panic or instability Dodd-Frank is designed to prevent. Such arguments have been accepted in other emergency contexts, but almost invariably with the caveat that a prompt post-deprivation hearing is available in which the legality of the seizure can be challenged and the property restored to its rightful owner if it turns out the seizure was unwarranted.[151] Justice Jackson, in *Fahey v. Mallonee*, described bank seizure as a "drastic procedure" justified by the "delicate nature of the institution and the impossibility of preserving credit during an investigation."[152] But the procedure at issue[153] provided for extensive hearing rights, including a full particularization of the reasons for the seizure, within a matter of days after the seizure took place.[154] Dodd-Frank's OLA, as amended by the Senate, *eliminates* the right of post-seizure judicial review routinely available (if rarely invoked) in the banking industry. Under Dodd-Frank, creditors who dispute the priority or valuation of their claim as determined by the FDIC can seek judicial review. But the government can point to no provision in the statute giving a post-seizure remedy to any other stakeholders, which will make it much more difficult to justify the absence of notice to these affected persons.

Beyond notice, due process concerns are also presented by the extremely abbreviated 24 hour period between the filing of the petition and the automatic granting of the petition required by Title II. Realistically speaking, it is impossible to imagine that this is adequate time either for the firm to mount an effective defense or for the court to engage in meaningful deliberation about the issues presented.[155] To be sure, the only issues the court is allowed to consider are whether the Secretary acted in an arbitrary and capricious fashion in determining that firm is a "financial

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[151] See, e.g., Mallen, supra, 486 U.S. at 24-41; Fahey v. Mallonee, 332 U.S. 255, 253-54 (1947); Coffin Bros. v. Bennett, 277 U.S. 29 (1928); North American Cold Storage Co. v. Chicago, 211 U.S. 306, 314-321 (1908).

[152] 332 U.S. at 253-54.

[153] The procedure being challenged in Fahey v. Mallonee was set forth in Section 5(d) of the Home Owners' Loan Act of 1933, as amended. See 12 U.S.C. §1464(d). This provision gave the Board of the Federal Home Loan Administration the authority to reorganize, consolidate, merge, or liquidate Federal Savings and Loan Associations, including the power to appoint a conservator or a receiver to take charge of the affairs of any such association. *Id.*

[154] 332 U.S. at 252-253.

[155] See Kenneth Scott, *Dodd Frank: Resolution or Expropriation* (2012) at http://media.hoover.org/sites/default-/files/documents/dodd-frank-20120302.pdf . "The Dodd-Frank Act squeezes pre-seizure due process down to the vanishing point." *Id.* at 1.

firm" as defined by the statute,[156] and whether he acted arbitrarily and capriciously in determining that the firm is in default or in danger of default.[157] But if these elements are contested, it is inconceivable that the firm could put together a coherent rebuttal, present it to the court, and that the court could digest the issues and render a well considered decision within such an extremely compressed time period. This is especially true of the finding that the firm is "in default or in danger of default."[158] This could entail an examination of hundreds of disputed accounting issues, many of great complexity.

The process is made more problematic by the lack of clarity about what the drafters of Dodd-Frank understood by an "arbitrary and capricious" standard of review. The APA directs courts to set aside agency action that is "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law." [159] This standard expressly encompasses questions of law as well as fact. Does the omission of the phrase "otherwise not in accordance with law" in Dodd-Frank mean that the district court may not review disputed questions of law? Such a construction would very likely be unconstitutional. [160] The fundamental objective of the Due Process Clause is to assure that the government deprives persons of their property only in accordance with the law, that is, "due process of law." An attempt by Congress to cut off any ability to challenge the lawfulness of a taking of property – at both the administrative and the judicial level -- would almost certainly contravene due process.

The statute's limitation of review to just two of the seven factors that the Secretary must consider in determining whether to petition for appointment of a receiver creates further due process problems. The statute requires the Secretary to petition for a receivership if he makes seven enumerated determinations listed in the statute.[161] There is no provision for an

[156] DFA, § 201(11). Financial firm means bank holding company, nonbank financial company supervised by the Federal Reserve Board, or any company or subsidiary of a company previously determined by the Fed to be predominately engaged in activities "financial in nature."

[157] As defined by DFA, § 203(c)(4), which sets forth four alternative conditions. Some of these conditions, such as that a bankruptcy case is likely to be promptly commenced, id. § 203(c)(4)(A), might be provable by documentary or testimonial evidence, and could conceivably be resolved in one day – provided the evidence was already in hand. But other conditions, such as that the firm "has incurred, or is likely to incur, losses that will deplete all or substantially all of its capital, and there is no reasonable prospect for the company to avoid such depletion," id. 203(c)(4)(B), would seem to require complex expert witness testimony that would be impossible to rebut or sort out in 24 hours.

[158] DFA § 203(b)1); 202(a)(1)(A)(iii).

[159] APA, 5 U.S.C. § 706(2)(A).

[160] See Crowell v. Benson, 285 U.S. 22 (1932); Richard H. Fallon, Jr., Of Legislative Courts, Administrative Agencies, and Article III, 101 Harv. L. Rev. 915, 943-49 (1988).

[161] DFA § 203(b).

administrative hearing on any of the seven issues. The statute provides for judicial scrutiny of only two of the seven determinations, in the 24 hour hearing previously described under the arbitrary and capricious standard of review. How is it possible for the government to seize and liquidate a major financial firm based on five determinations that are never subject to any challenge by the targeted firm? Welfare recipients cannot have their benefits terminated based on determinations made by social workers that the beneficiary is never allowed to contest.[162] Why should financial firms be liquidated without any opportunity to contest the legal determinations that support this action? Some determinations required by Dodd-Frank involve discretionary determinations of the legislative fact variety, such as the finding that resolution of the firm under ordinary bankruptcy law "would have serious adverse effects on financial stability in the United States." [163] But others are highly factual, in the adjudicatory fact sense, e.g., that the financial firm has been ordered to convert all convertible debt instruments.[164] Eliminating all avenues of challenging these determinations, either ex ante or ex post, seems hard to justify as being consistent with due process.

Is it possible to defend the extremely limited review provided by Title II based on the government's paramount interest in preventing financial meltdown? The general due process standard for procedural adequacy is the balancing test of *Mathews v. Eldridge*,[165] which focuses on three variables: (1) the "private interest that will be affected by the official action"; (2) the "risk of an erroneous deprivation of such interest through the procedures used, and the probable value, if any, of additional or substitute procedural safeguards;" and (3) "the Government's interest, including the function involved and the fiscal and administrative burdens that the additional or substitute procedural requirements would entail." The magnitude of the private interest at stake will depend on who is bringing the challenge. The firm and its directors and shareholders may have the weightiest interests. The statute mandates that any firm placed in an OLA receivership must be liquidated and that all shareholder equity must be wiped out before other creditors take a hit. Directors are subject to mandatory dismissal. Directors of systemically significant financial firms may not elicit as much sympathy from the courts as welfare recipients and school janitors,[166] but directorships are paid positions and under the statute the critical decision that determines whether a director keeps or loses her position is the

[162] Cf. Goldberg v. Kelly, 397 U.S. 254 (1970) (requiring elaborate hearing before welfare benefits are terminated).

[163] DFA § 203(b)(2).

[164] DFA § 203(b)(6).

[165] Mathews v. Eldridge, 424 U.S. 319, 335 (1976).

[166] See Goldberg v. Kelly, 397 U.S. 254 (1970) (welfare recipients are entitled to adjudicatory hearing before benefits are terminated given "brutal need" eligible recipients have for such funds); Loudermill, supra (school janitor with undisclosed criminal record entitled to hearing before termination given importance of employment to individual welfare).

appointment of receiver. Once this happens, all directors are automatically terminated.[167] Creditors will have more difficulty arguing that their interest is large, given that Title II gives creditors the right to bring a judicial proceeding to determine the validity of their claims, and establishes a benchmark for compensation equal to what a claimant would receive in a liquidation of the firm.[168] Officers who fear they will be dismissed may be met with the argument that any consideration of this prospect at the time of appointment of a receiver is premature. Dismissal of officers is required only if they are found to be "responsible for the failed condition of the covered financial company"[169] and thus any challenge by officers may not be ripe until the FDIC determines they warrant dismissal.

The Government will undoubtedly argue that the procedures prescribed by Title II serve governmental interests of the highest magnitude. The very short notice and rocket-like hearing are not designed to save on administrative costs, but to prevent a financial panic or contagion analogous to a run on the bank if ordinary judicial procedures were followed. In order to prevent future financial crises caused by the collapse of nonbank financial firms that are too big to fail, Congress determined that the government must be able to seize and liquidate major financial firms in an expeditious, in camera process. Stated in these terms, it is difficult to see how the interests of a single firm or its shareholders and directors in avoiding liquidation can be regarded as outweighing the prevention of an economic crisis. Forced to choose patent unfairness and economic disaster, courts will likely acquiesce in patent unfairness.

Notice, however, that the *Mathews* test appears to contemplate a marginalist inquiry. The primary question is not whether the totality of the private interest outweighs the totality of the governmental interest, but whether "additional or substitute procedural safeguards" would be worth more or less than the "fiscal and administrative burdens that the additional or substitute procedural requirement would entail."[170] In the context of an OLA petition, this implies, for example, that the court should ask whether affording a financial firm, say, an additional 24 hours to mount a defense (with the proceedings remaining under seal) would be worth more in terms of preventing unfairness than the cost to the government and society in terms of increasing the risk of financial disaster. There is, of course, no meaningful way in which a court can answer such a question. This is a problem associated with the risk-utility due process test of *Mathews* more

[167] DFA § 206(5).

[168] DFA, §

[169] DFA 206(4).

[170] Mathews, 424 U.S. at 335.

generally.[171] But posing the question this way would at least increase the odds that the court would agree the statute violates due process.

Given the intractable nature of the *Mathews* balancing test, especially as applied to such a high stakes situation, it is virtually certain that the parties and the court would look to analogous processes in order to decide whether Title II comports with due process. In particular, the government would inevitably emphasize that existing bank receivership laws allow regulators to seize banking companies with no advance judicial process at all.[172]

The problem with this analogy is twofold. First, as emphasized above, the banking statutes provide for de novo judicial review *after* the seizure takes place. Both the Administration's proposed version of OLA and the House bill followed this model, and provided for unrestricted judicial review after the seizure of a systemically significant nonbank financial firm. The Senate, for whatever reasons, eliminated post-seizure review and substituted the extremely limited one-day pre-seizure review limited to just two issues. In so doing, it made it far more difficult to defend the statute against a due process challenge.

Second, the rationale for dispensing with ex ante procedures in the bank receivership context depends in significant part on a quid pro quo or waiver argument keyed to government deposit insurance. The leading precedent is *Fahey v. Mallonee*,[173] which presented a constitutional challenge to the takeover of federally-chartered savings and loan association by the Federal Home Loan Bank Board.[174] Justice Jackson not only alluded to the heightened need for public regulation of banks, given their vulnerability to panics and the impact this can have on the wider economy. He also reasoned that the savings and loan in that case was "estopped" from challenging the law because it had voluntarily sought a federal charter, knowing that a takeover was a possibility if the Bank Board became concerned about its financial condition. As he put it: "It would be intolerable that the Congress should endow an association with the right to conduct a public banking business on certain limitations and that the Court at the behest of those who took advantage from the privilege should remove the limitations intended for public protection."[175]

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[171] See, e.g., Jerry L. Mashaw, Administrative Due Process as Social-Cost Accounting, 9 Hofstra L. Rev. 1423 (1981).

[172] 12 C.F.R. 30, FDIC's Notice of Proposed Rulemaking Implementing Certain Orderly Liquidation Authority Provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act (March 15, 2011).

[173] 332 U.S. 245 (1947).

[174] The challenge was grounded in the nondelegation doctrine, but the Court addressed the limited procedural protections in its analysis.

[175] 332 U.S. at 256.

The quid pro quo theme has recurred in more recent cases addressing due process challenges to various administrative actions taken by bank regulators, often with emphasis on the government benefit of deposit insurance, which greatly promotes public confidence in the banking system.[176] Ordinary bank receiverships and related summary actions occur in a context in which the most significant assets of the insolvent bank – the deposits that have been made by its customers – are insured by the federal government. This gives the federal government a very large justification for moving quickly and without advance notice to take over an insolvent bank in order to limit the government's exposure on its insurance obligations. It also allows the government to say that the bank voluntarily assumed the risk of summary action in return for taxpayers largely footing the bill for any missteps or even misconduct by the bank. The banks, one could say, must take the bitter with the sweet.[177]

This sort of quid-pro-quo argument cannot be easily extended to the nonbank financial firms subject to orderly liquidation under Title II.[178] Large non-bank financial firms are not chartered by the government, and do not have anything like the close interaction with regulatory agencies that characterizes banks. They may be subject to oversight by the SEC or the CFTC, but this does not rise to the level of intensity of scrutiny associated with visitorial authority regulators exercise over banks. And of course the government does not formally insure funds and investments held by clients in these nonbank financial firms. Perhaps TARP and the bailout regime could be characterized as one in which the government implicitly guaranteed that systemically significant firms will not be allowed to fail. But Title II is designed to *eliminate* such a guarantee – to make sure the government will never again foot the bill for any capital infusions required by the resolution process. It is much more difficult in this context to claim that the government has delivered enough of the "sweet" to say that firms liquidated under Title II have voluntarily assumed the risk of getting the "bitter." Consequently, it is implausible that the OLA can be justified by the kind of estoppel argument adopted in *Fahey v. Mallonee*.

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[176] FDIC v. Mallen, 486 U.S. 230 (1988) (rejecting due process challenge to rule requiring automatic suspension of bank official indicted for crime); James Madison Ltd. V. Ludwig, 82 F.3d 1085 (D.C. Cir. 1996) (rejecting due process challenge to actions by OCC and FDIC declaring bank holding company insolvent and seizing assets); Bd. of Governors of Federal Reserve Sys. v. DLG Financial Corp., 29 F.3d 993 (5th Cir. 1994) (rejecting due process challenge to preliminary injunction freezing assets of shareholder of corporation for possible violations of Bank Holding Company Act); FDIC v. Bank of Coushatta, 930 F.2d 1122 (5th Cir. 1991) (holding capital directive to bank was unreviewable and that the administrative process that produced the directive and the enforcement order satisfied due process); Spiegel v. Ryan, 946 F.2d 1435 (9th Cir. 1991) (rejecting due process challenge to temporary cease and desist order requiring restitution of $21 million by bank officer pending administrative review); FDIC v. Haralson v. Federal Home Loan Bank Bd., 837 F.2d 1123 (D.C. Cir. 1988) (rejecting due process challenge to appointment of conservator under statute providing for review only after seizure of assets).

[177] Cf. Arnett v. Kennedy, 416 U.S. 134, 152-54 (1974), rejecting a bitter with the sweet argument in the context of a due process challenge. Id. at 166-67 (Powell, J.); id. at 177-78, 185 (White J.); id at 211 (Marshall, J.).

[178] See Zaring, supra, 60 Emory L. J. at 129-30.

Sadly and ironically, the extremely short notice required by the statute will itself produce a litigational advantage for the government that will be extremely difficult to overcome. The government can prepare briefs in advance suggesting the sky will fall if a systemically significant firm is not placed in receivership immediately. The government can also anticipate a due process objection, and can have its briefs, complete with extensive citations to banking cases and public health emergencies, prepared well in advance. The financial firm may be caught by surprise, and find it nearly impossible to rebut these authorities. The violation of due process may itself assure that the due process defense fails. Certainly this will be true for stakeholders who receive no notice at all until the receivership is approved.

The last point to make in connection with the serious due process issues raised by Title II is that they were almost certainly avoidable if Congress had simply followed the Administration draft and the House bill in providing for administrative appointment of a receiver followed by a statutory right to post-seizure judicial review. It is well established that some form of hearing is required before a property owner is conclusively deprived of a protected property interest.[179] That said, it does not necessarily follow that the hearing must occur before the initial taking occurs.[180] Specifically, the timing, nature and procedural requirements of any mandatory hearing under due process clause will depend on a balancing of the competing interests involved, including the importance of the private interest and length or finality of the deprivation at issue, the probability of government error and the importance of governmental interests involved, including the administrative practicality of providing a hearing ex ante and the sufficiency of substitute procedure ex post.[181] Given the substantial public interest in avoiding a financial panic, and the practical constraints on providing advance notice to the numerous creditors with property interests at stake given the need for expedition, it is hard to imagine a court finding ex post review unjustified.

As we have seen, for practical reasons banks only rarely invoke their right to seek post-seizure review. But the availability of such review is an important safeguard against executive abuse of the enormous power conferred by Title II. Post seizure review eliminates the notice problem, because the entire world will know about the appointment of the receiver. And it eliminates the need to ram the proceeding through in 24 hours or to truncate the issues so that only a fraction of the potential points of legal contestation are subject to review. The Senate

[179] See Logan v. Zimmerman Brush Co., 455 U.S. 422, 433-434 (1982); Fuentes v. Shevin, 407 U.S. 67, 80-82 (1972).

[180] See Memphis Light, Gas and Water Division v. Craft, 436 U.S. 1, 19 (1978); Ingraham v. Wright, 430 U.S. 651, 680 (1977); Bragg v. Weaver, 251 U.S. 57, 62 (1919).

[181] Matthews, 424 U.S. at 339-349 (1976); FDIC v. Mallen, 486 U.S. 230, 240-241 (1988).

blundered in thinking that a sham review before appointment of a receiver is preferable to a right to plenary review afterwards.

B. Article III.

The extremely compressed process for obtaining a judicial order establishing an FDIC receivership is also vulnerable to challenge on Article III grounds. Indeed, the Article III objection may strike an even more sympathetic cord with courts than the due process claim, because it implicates the constitutional authority and autonomy of the courts as a separate branch of government.

We hasten to point out that the Article III issue is not the one typically associated with bankruptcy laws, as in *Stern v. Marshall* [182] or *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*[183] In those cases, the Court was concerned with whether the Bankruptcy Court – an Article I tribunal – could resolve what were concededly claims of private right under the common law of contract and tort subject only to deferential review by an Article III district court. The initiation of a Dodd-Frank OLA proceeding, in contrast, would almost surely be classified as one involving public rather than private rights.[184] An OLA action is commenced by a federal official, the Secretary of the Treasury, and it seeks the appointment of a federal agency (typically the FDIC) as receiver. The decision to grant the petition and the standards for conducting the receivership are governed by federal, not by state law. The rationale for the action is grounded in general considerations of the public interest -- to prevent a contagion or panic that would disrupt financial markets and lead to economic distress – not the resolution of claims between private debtors and creditors. The receivership will of course result in the resolution of numerous private claims, but this is secondary or incidental to its primary purpose. Thus, although the Supreme Court has failed to identify any bright line distinction between private and public rights, the OLA action seems rather clearly to fall on the public side of the line. The Court has repeatedly affirmed that public actions need not be tried in Article III courts; Congress has the option of conferring them on either Article III courts or administrative tribunals.[185]

[182] No. 10-179, June 23, 2011.

[183] 458 U.S. 50 (1982).

[184] Thus, we question the analysis in Brent J. Horton, How Dodd-Frank's Orderly Liquidation Authority for Financial Companies Violates Article III of the United States Constitution, 36 J. Corp. L. 369 (2011), which implicitly treats the appointment of a receiver as a matter of private right for Article III purposes.

[185] Murray's Lessee v. The Hoboken Land and Imp. Co., 59 U.S. (18 How.) 272 (1855); Crowell v. Benson, 285 U.S. 22 (1932).

Moreover, in contrast to the claims at issue in *Marshall* and *Northern Pipeline*, the decision to appoint a receiver and initiate a liquidation of a financial firm *is* formally made by an Article III court – the District Court for the District of Columbia -- not by an administrative body or an Article I court. The statute says: "If the Court determines that the determination of the Secretary [on the two reviewable determinations] is not arbrtrary and capricious, *the Court* shall issue an order immediately authorizing the Secretary to appoint the Corporation as receiver of the covered financial company."[186] There is no attempt here to transfer authority away from an Article III court and give it to some other tribunal. The authority to appoint the receiver is formally exercised by the district court.[187] And the statute further elides traditional *Northern Pipeline*-type problems by providing that creditors of the financial firm subject to OLA, if they are dissatisfied by the receiver's resolution of their claims, can bring an action in federal district court and have their claim resolved there. [188] The statute appears to contemplate that these judicial proceedings will be tried de novo, not under a standard of deferential administrative review.

The principal Article III problem we have in mind, rather, is whether a statute that severely restricts an Article III court in terms of the time it is given to consider an important question as well as the scope of the issues it can consider in resolving the question violates Article III. (Perhaps this might be called a separation of powers issue, rather than an Article III issue, to avoid confusion with *Northern Pipeline*-style claims.) In effect, the statute calls upon an Article III court to make a decision of surpassing importance, both to the financial firm and the economy, and yet simultaneously constrains the court to make this decision in such a way that it cannot discharge this duty in a manner consistent with the judicial power established by Article III. One might say that Dodd-Frank commandeers the court to lend its prestige and legitimacy to what is essentially an administrative process without respecting the traditional mode and manner in which courts function.[189] In our view, any court told that it must approve or reject a petition to establish a receivership to liquidate a huge financial firm, and that it has only 24 hours to consider the question, will be very uneasy with its appointed role.

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[186] DFA § 202(a)(1)(iv) (emphasis added).

[187] The matter is admittedly murkier if the district court fails to act within 24 hours. The statute switches to the passive voice and declares that "the petition shall be granted by operation of law" and then adds: "the Secretary shall appoint the Corporation as receiver." DFA § 202(a)(1) (v) (I) & (II). At least arguably, the Secretary is the appointing authority in these circumstances.

[188] DFA § 210(a)(4).

[189] Cf. Printz v. United States, 521 U.S. 898; New York v United States, 505 U.S. 144 (principles of federalism do not permit Congress to commandeer state governments to act as enforcement agents of federal law).

One sign of judicial discomfort is found in the D.C. District Court's Local Rule 85, which was amended to implement Dodd-Frank's in camera procedure for appointment of a receiver.[190] The new Rule provides in part that "[a]t least 48 hours prior to filing the petition, the Secretary shall provide written notice under seal to the Clerk of the Court that a petition will likely be filed with the Court." There is no authority for this advance notice requirement in the statute, although presumably the Treasury will attempt to comply with it. The additional 48 hour notice is evidently designed to facilitate assignment of a judge to the matter and to allow the judge to clear his or her docket for the 24 hour marathon to come. This will relieve some pressure from the judge who must decide the matter, although the content of the petition itself, as well as any objections by the financial firm, will not be made available until the 24 hour clock starts ticking. Local Rule 85 cannot obviate the reality that a single judge must decide whether to order the liquidation of a systemically significant financial firm in a process that is the equivalent of a law school take-home examination.

The Article III objection is exacerbated by the statute's restriction of the court to considering two of the seven threshold determinations that must be resolved before an OLA receivership is established. The court is to consider only whether the Secretary of the Treasury acted arbitrarily and capriciously in finding that the firm met the statutory definition of a "financial company," and whether he acted arbitrarily and capriciously in finding that the firm "is in default or in danger of default." The other five statutory triggering conditions are, according to Dodd-Frank, not to be considered by the court. Yet the judgment the court is asked to render – granting a petition to appoint a receiver leading to mandatory liquidation – necessarily presupposes that all statutory triggering conditions have been met. The court may be uncomfortable rendering a judgment that rests on legal and factual determinations it is not empowered to review. Again, the objective of the statute appears to be to draw upon the prestige of the court as an independent tribunal to legitimize a process that is actually driven by the executive. Courts will not take kindly to being conscripted in this fashion.

There is little precedent to draw upon in considering the Article III claim. The matter is arguably analogous to *Hayburn's Case*,[191] where the courts were asked to render judgments subject to revision by the Executive. This was condemned on the ground that it made the judgments nothing more than advisory opinions.[192] Arguably the same conclusion should follow when the Executive renders a decision that the court is asked to incorporate into a judgment, but without being given the time or the authority to make an independent determination of fact and

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[190] See Local Civil Rule 85 supra note 97.

[191] 2 U.S. (2 Dall.) 408 (1792).

[192] See Richard H. Fallon, Jr., Hart & Wechsler's The Federal Courts and the Federal System 83-90 (6th ed. 2009) (explaining the significance of *Hayburn's Case* for understanding of the role of Article III courts).

law necessary to render a proper judicial judgment. The judicial input in both instances lacks substance, and serves only to transfer a measure of judicial prestige to an executive enterprise. Justice Douglas once warned that a statute which makes "the federal judiciary a rubber stamp for the President" would violate Article III.[193] "If the federal court is to be merely an automaton stamping the papers and Attorney General presents," he wrote, "the judicial function rises to no higher than an IBM machine."[194] His colleagues disagreed with his interpretation of the statute under review, but not with his understanding that such a statute would violate Article III.

The absence of meaningful precedent to assess the Article III claim is both a strength and a weakness. It is a strength insofar as Congress has never before attempted to draw upon the authority of the courts while simultaneously constraining their ability to function as a court in such a dramatic fashion. The unprecedented nature of the judicial appointment provisions of Title II make it suspect. It is a weakness insofar as there is a presumption in favor of the constitutionality of duly-enacted legislation, and courts like to draw upon clear constitutional language or settled authority before rendering a judgment at an enactment of Congress is unconstitutional.

The provisions authorizing an appeal from a district court order appointing a receiver raise further Article III questions. If the district court grants the petition to appoint a receiver, or if the petition is granted as a matter of law because the district court fails to act within 24 hours, the statute says the decision "shall be final, and shall be subject to appeal only in accordance with" the appeal provisions of Title II.[195] The Act then adds: "The decision shall not be subject to any stay or injunction pending appeal."[196] If this last sentence is interpreted to mean that the Court of Appeals (and the Supreme Court on further petition for certiorari) have no authority to enjoin or set aside the decision of the district court once it becomes final, then the "appeal" would have no function other than to render an advisory opinion as to whether the district court acted correctly. This would be a plain violation of Article III. To avoid this conclusion, one must hone in on the word "pending" in the sentence that prohibits any stay or injunction "pending appeal." This should be interpreted to mean that no stay or injunction can be entered while the appeals are *pending*, but once the appeals process is *final*, the appeals court and the Supreme Court have authority to enjoin or set aside the district court decision if they conclude that the Secretary acted arbitrarily and capriciously.[197] As interpreted, this creates a strange go-

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[193] United Steelworkers of America v. United States, 361 U.S. 39, 71 (1959) (dissenting opinion).

[194] Id.

[195] DFA, §202(a)(1)(B).

[196] DFA, § 202(a)(1)(B).

[197] We thank Ron Levin for pointing out this problem and its possible solution.

and-stop judicial review process, but this is little different from the post-seizure review provisions of the banking receivership laws, which likewise presume that a receivership can start and then be stopped on an ex post petition for review to a court.

If the statute is interpreted as allowing the Court of Appeals or the Supreme Court to overturn a receivership on appeal or certiorari, and it imposes no time limit on the Court of Appeals or the Supreme Court in reaching the determination whether the Secretary's two findings are arbitrary and capricious, does this solve the Article III problem? It clearly means that these two courts would not be dragooned into rendering decisions in a time period too compressed to allow them to act in a properly judicial fashion. But it would still leave the district court dragooned to act in a manner impossible to discharge in a proper judicial manner. And it would limit the Court of Appeals and the Supreme Court to considering only two of the seven factors that determine whether the Secretary must petition for a receivership. As previously discussed, this presents an independent due process problem, and might be construed as presenting an Article III problem as well, insofar as the Appeals Court and the Supreme Court are being asked to restrict their review to only a subset of the legal issues that lead to the appointment of a receiver. Arguably this too represents an attempt by Congress to exploit the prestige of the judiciary while preventing it from discharging its judicial function in a proper manner.

Can the district court avoid any insult to its judicial independence by simply declining to rule on the petition, in which case it takes effect by operation of law in 24 hours?[198] This would preserve the dignity of the district court, by refusing to lend its prestige to a process that forces the court to act in a non-judicial manner.[199] But the financial firm could still appeal, in which case the Article III question about limiting the courts to reviewing two of seven determinations would still be presented. More seriously, refusing to rule would spare the court at the expense of the parties subject to orderly liquidation. Indeed, by declining to participate, the court would only exacerbate the due process problem. Not only would the parties be denied any post-seizure judicial review, they would not even get the extremely abbreviated pre-seizure review provided by the statute. Seizure of systemically significant financial firms would take place based on the unreviewable say-so of the Executive.

C. Avoidance Anyone?

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[198] The Dodd-Frank Act requires the District Court to adopt rules implementing the judicial appointment provisions of the Act. See note 97 supra.

[199] Cf. Korematsu v U.S. 323 US 214, 246 (Jackson, J. concurring) (urging that the Court refrain from upholding or overturning the use of internment camps to avoid establishing a precedent).

Before concluding our consideration of process objections to Title II, another wrinkle should be considered, namely, whether the statute can be construed in such a way as to eliminate the constitutional problem. The potential avoidance move here might be to find that although Dodd-Frank severely limits what the court can consider and how it must consider it, the APA can step in to supplement the court's reviewing authority, and in so doing eliminate possible due process and Article III problems.

Recall again that the statute requires the Secretary to make seven determinations before seeking the appointment of a receiver, and allows the district court to review only two of these determinations. Is it possible that a financial firm facing the appointment of a receiver could obtain review of the other five determinations under the APA – without being shackled by the 24 hour time limit and the arbitrary and capricious standard of review? The APA provides that "[a]gency action made reviewable by statute and final agency action for which there is *no other adequate remedy in a court* are subject to judicial review."[200] This would seem to fit the supposed situation, insofar as there is no other adequate remedy in court if the Secretary has committed legal or factual error with respect to five of the seven determinations. Indeed, insofar as the Dodd-Frank review provisions constrain the court with respect to the two determinations made reviewable – imposing a time so short it effectively deprives a firm of any adequate remedy in court – one could argue that all seven determinations can be reviewed under the APA because the review process prescribed by Dodd-Frank is plainly not "adequate."

Can we say the Secretary's decision to file a petition is "final agency action?" The Supreme Court has instructed that "two conditions must be satisfied for agency action to be 'final': First, the action must mark the consummation of the agency's decision making process…[and] must not be of a tentative or interlocutory nature. And second, the action must be one by which rights or obligations have been determined, or from which legal consequences will flow."[201] The first factor would seem clearly to be met. The Secretary's decision making process culminates in filing a petition to appoint a receiver; he bows out at that point and turns everything over to the court and the FDIC. The second factor is more problematic. In formal terms, the court appoints the receiver, not the Secretary. So the "legal consequences" (which are considerable) flow from the court's decision to grant the petition, not the Secretary's decision to file it. Realistically speaking, however, the Secretary's decision is the one that matters. The court has only very limited grounds for rejecting a petition (and then only by remand to the Secretary for further findings), and only 24 hours to do so. One way to resolve the matter is to focus on the way the statute handcuffs the court by permitting it to review only two of the seven determinations that the Secretary must make before filing a petition. As to the remaining five factors, the Secretary's decision is the last word. As to these factors, the Secretary's decision is

[200] APA, 5 U.S.C. § 704.

[201] Bennett v. Spear, 520 U.S. 154, 177-78 (1997).

fully and effectively "final," since the Dodd Frank Act provides for review by the court of only the other two factors. And the factors that are unreviewable under the Dodd Frank Act are the critical ones the financial firm would ask the court to review under the APA.

A more serious problem is presented by Section 701(a) of the APA, which exempts matters from APA review when "statutes preclude judicial review" or "agency action is committed to agency discretion by law."[202] The government would surely move to dismiss any action seeking review of the five determinations (or all seven) under the APA on the ground that the statute makes them unreviewable. Absent a constitutional avoidance issue, we would regard this as a dispositive objection. The statute does not expressly preclude review of the five determinations. It does say, however, that the district court can only consider two determinations. And the appeals court and the Supreme Court are expressly limited to the two determinations. Courts sometimes say that the inclusion of one type of review should be implicitly regarded as exclusion of other types of review,[203] and that inference is particularly strong under the wording of Dodd-Frank. Once the constitutional avoidance issue is added to the mix, however, it becomes a closer call. Given the substantial due process and Article III arguments that the Dodd-Frank review provisions are unconstitutional, a court would likely strain mightily to avoid such a conclusion by finding that APA review has not been precluded, and that APA review can supplement the procedural deficiencies under Dodd-Frank. A sensible court would of course seek to harmonize APA review with the congressional judgment that the appointment of a receiver must be resolved quickly and confidentially; so the court would set a timetable for APA review that requires considerable dispatch and keeps the matter under seal at least until a final judgment is reached.

The government might also argue that even if review of the five determinations is not precluded by statute, these determinations are committed to agency discretion by law. One common refrain here is that matters are presumptively reviewable as long as there is "law to apply."[204] The five determinations Dodd-Frank sets out for the Secretary to consider (in addition to the two made reviewable by the district court) vary in terms of whether they point more toward a purely discretionary determination by the Secretary or the application of law to fact. Whether the failure of a financial firm would have "serious adverse effects on financial stability in the United States"[205] would seem to be a determination one would want the Secretary of the Treasury to make, not an Article III court. On the other hand, whether "a Federal regulatory agency has ordered the financial firm to convert all of its convertible debt instruments that are

[202] APA, 5 U.S.C. 701(a).

[203] E.g., Block v. Community Nutrition Inst., 467 U.S. 340 (1984).

[204] E.g., Webster v. Doe, 486 U.S. 592 (1988); Citizens to Preserve Overton Park v. Volpe, 401 U.S. 402 (1971).

[205] DFA, § 203(b)(2).

subject to the regulatory order"[206] seems to be abundantly one as to which there is "law to apply." As long as at least one contested determination includes debatable issues of law or fact of the sort that courts often adjudicate, the committed to agency discretion argument would fail, at least in part. Again, the need to avoid deeply unsettling constitutional questions might well tip the balance in favor of finding that at least some determinations are not committed to agency discretion by law.

One potential difficulty with using the APA as an avoidance mechanism would arise if the financial firm subject to a petition for liquidation did not invoke the APA as a basis for review – something easy to overlook if a defense must be organized in less than 24 hours. Perhaps the court could raise this on its own motion, in the interest of avoiding constitutional difficulties. But it would be desirable for the financial firm to ask the court to review the petition under the APA as well as under the Constitution.

IV. Constitutional Issues – Substantive Objections

Dodd-Frank's orderly liquidation authority may be vulnerable on other constitutional grounds that implicate the authority of Congress to mandate the kind of receivership contemplated by Title II. This section looks at two possible Constitutional objections – one grounded in the uniformity requirement of the Bankruptcy Clause and another based on the First Amendment.

A. Uniform Laws of Bankruptcy.

The Constitution confers power on Congress to adopt "uniform Laws on the subject of Bankruptcies throughout the United States."[207] One possible objection to the Dodd-Frank OLA is that it does not constitute a uniform bankruptcy regime. Instead, the government is instructed to determine, on a case-by-case basis, whether to subject a nonbank financial firm to ordinary rules of Bankruptcy, or to switch the firm over to a different track reserved for systemically significant nonbank financial firms. The result is different bankruptcy laws for different financial firms, based on a highly discretionary determination by executive branch agencies as to which is more appropriate. The fact that Title II contains elements significantly more punitive than the ordinary bankruptcy regime makes this discretionary authority especially problematic. A distinct uniformity objection to OLA is that the statute authorizes the FDIC as receiver to treat similarly-situated creditors differently, if it determines that this is necessary to maximize the value of the assets of the firm, initiate or continue operations essential to receivership, or

[206] DFA, § 203(b)(7).

[207] U.S. Const. art. I, § 8, cl. 4.

minimize losses.[208] As we have seen, the state plaintiffs in *Big Spring* cite this potential lack of uniformity as grounds for establishing their standing to challenge the constitutionality of Dodd-Frank.

The reason for the limitation to "uniform laws" in the Bankruptcy Clause is not entirely clear.[209] The leading case, *Railroad Labor Executives Assoc. v. Gibbons*, [210] construed the limitation to mean that Congress has no power to enact a law reorganizing a single debtor. Thus, if Congress were to enact a special law prescribing an orderly liquidation procedure applicable only to a single non-bank financial firm this could be challenged as an unconstitutional exercise of the bankruptcy power under the authority of *Gibbons*. The question is whether a similar conclusion should follow when Congress prescribes a specialized form of bankruptcy for financial firms and gives the executive branch broad discretion to apply this specialized regime rather than otherwise-uniform bankruptcy rules on a case-by-case basis.

In *Gibbons*, the Supreme Court considered the Rock Island Railroad Transition and Employee Assistance Act (RITA), a law passed specifically to address the circumstances of the Rock Island Railroad bankruptcy.[211] Among other things, the law sought to require that the railroad's bankruptcy trustee provide certain economic benefits to railroad employees who were not hired by other railroad carriers. In considering whether this special law was constitutional, the Court addressed two issues. First, whether the Act should be regarded as having been passed pursuant to the Bankruptcy Clause, which requires that laws be "uniform," or could be regarded as having been passed pursuant to the Commerce Clause, which does not include a uniformity requirement.[212] Second, whether the uniformity requirement of the Bankruptcy Clause prohibits a bankruptcy law that applies to only one debtor.

The first issue – whether RITA was enacted pursuant to the Bankruptcy Clause or the Commerce Clause – was critical, because the Court recognized that "if we held that Congress had the power to enact nonuniform bankruptcy laws pursuant to the Commerce Clause, we would eradicate from the Constitution a limitation on the power of Congress to enact bankruptcy laws."[213] It was therefore necessary to determine whether RITA fell within the ambit of the

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[208] DFA, 210(b)(4).

[209] The Federalist Papers contain only one sentence about the Bankruptcy Power. See The Federalist No. 42 (Madison) (noting that "[t]he power of establishing uniform laws of bankruptcy, is so intimately connected with the regulation of commerce, and will prevent so many frauds where the parties or their property may lie, or be removed into different states, that the expediency of it seems not likely to be drawn into question.")

[210] 455 U.S. 457, 471 (1982).

[211] 455 U.S. at 462-63.

[212] Id. at 468.

[213] Id. at 469.

bankruptcy power. After surveying its prior decisions, the Court concluded that the bankruptcy power "extends to all cases where the law causes to be distributed, the property of the debtor among his creditors."[214] The power "includes the power to discharge the debtor from his contracts and legal liabilities, as well as to distribute his property."[215] In short, the Court held that any law that discharges the contracts and other legal liabilities of a debtor and distributes the property among creditors is a law adopted pursuant to the bankruptcy power. Under the rationale of *Gibbons*, Title II of Dodd-Frank would have to be regarded as being adopted pursuant to the Bankruptcy Power, and thus is subject to the "uniform laws" requirement.

With respect to the second issue, the Court acknowledged that the uniformity requirement of the Bankruptcy Clause "is not a straightjacket that forbids Congress to distinguish among classes of debtors, nor does it prohibit Congress from recognizing that state laws do not treat commercial transactions in a uniform manner."[216] It also acknowledged that Congress could take into account differences that exist between different parts of the country, and fashion legislation to deal with geographically isolated problems, as it had done in the Conrail bankruptcy.[217] But RITA was a different matter: "The employee protection provisions of RITA cover neither a defined class of debtors nor a particular type of problem, but a particular problem of one bankrupt railroad. Albeit on a rather grand scale, RITA is nothing more than a private bill such as those Congress frequently enacts under its authority to spend money."[218] The Court concluded that "[t]he language of the Bankruptcy Clause itself compels us to hold that such a bankruptcy law is not within the power of Congress to enact."[219]

The Court reinforced this conclusion by examining the history of the Bankruptcy Clause. The Clause was added to the Constitution during deliberations about the problem of affording full faith and credit to the legal actions of other states. Several states had followed the practice of passing private bills to relieve individual debtors, and questions had been raised about whether other states were obliged to recognize relief given by these acts. The Court concluded that the Bankruptcy Clause was adopted to provide Congress with the power to enact uniform

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214 Id. at 466, quoting *Hanover National Bank v. Moyses*, 186 U.S. 181, 186 (1902).

215 Id., quoting *Hanover National Bank*, supra, at 188.

216 Id. at 469.

217 *See Regional Railroad Reorganization Act Cases*, 419 U.S. 102, 159 (1974).

218 *Gibbons*, supra, at 470-71.

219 Id. at 471.

bankruptcy laws enforceable among the states, and that "the Bankruptcy Clause's uniformity requirement was drafted in order to prohibit Congress from enacting private bankruptcy laws."[220]

In light of *Gibbons*, it would be unconstitutional for Congress to enact a law providing special rules applicable solely to the resolution of a specific nonbank financial firm. The same result should follow if Congress delegates authority to the executive branch to adopt specialized rules for the re-organization of a single nonbank financial firm. Congress cannot delegate power to an agency that will overcome a limitation on Congress's own authority to act.[221] Is this Dodd-Frank? Given the extraordinary discretion that the Treasury Department and allied federal agencies have in determining that a financial company should be reorganized under Title II, as opposed to general bankruptcy laws, it certainly comes close. Title II's OLA may never be invoked, or may be invoked so rarely that it is tantamount to a one-off bankruptcy regime. And the decision whether to apply such a regime will left almost entirely to the discretion of the executive branch, under a statute that makes most of its determinations unreviewable.

There is, however, a distinction between Dodd-Frank and a bankruptcy regime that amounts to a private bill. After Dodd-Frank, there are two bankruptcy laws for large nonbank financial firms -- one for most nonbank financial firms (the Bankruptcy Code) and the other for firms deemed by the executive to be too big to fail (Dodd-Frank Title II). Congress has enacted both laws, and they are set forth in the form of general statutes. Congress has further instructed the executive to decide, on an ad hoc basis, which of the two packages of bankruptcy rules should apply in individual cases. If Congress had set forth clear legal criteria for determining when Package A applies as opposed to Package B, and had allowed ordinary judicial review of any decision as to which package to apply, we think this would probably be constitutional. After all, Congress has legislated different approaches to the resolution of insolvency in different industries, like railroads, banks, and insurance companies. This inevitably presents classification questions, which have been resolved using ordinary tools of statutory interpretation.

Dodd-Frank is a less clear case, because the factors for deciding which package of rules apply are highly discretionary and, as previously discussed, the provisions for judicial review are severely truncated. Congress came close to saying: here is a new package of bankruptcy rules for firms that are too big to fail, and you (the executive) decide in your unreviewable discretion which firms fall into that category.[222] It is difficult to describe this as a "uniform law" of

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[220] Id. at 472.

[221] See, e.g., Whitman v. American Trucking Assns., 531 U.S. 457, 473 (2001) (making this point in the context of a nondelegation challenge).

[222] A constitutional purist might insist that Dodd-Frank gives so much discretion to the executive in this regard that it violates the nondelegation doctrine. We do not pursue this inquiry here, because the Court has refused to find a nondelegation violation provided Congress has laid down any kind of standard to govern executive decision making. E.g., Whitman, supra; Fahey v. Mallonee, supra. Dodd-Frank sets forth seven "determinations" that must be made before a receivership is commenced, which is more than enough to meet the lax requirements of the contemporary

bankruptcy, but it presents a different order of problem from the statute invalidated in *Gibbons*. So the uniformity objection would sail into largely uncharted waters. Given that Dodd-Frank sets forth a general regime for resolving the bankruptcy of firms that are too big to fail, and does not seek to dictate special treatment for specific classes of creditors in pending cases, we doubt that the courts would extend *Gibbons* to reach this situation. But the argument cannot be said to be frivolous.

What then about the other uniformity problem cited by the plaintiffs in *Big Spring*: the provision of Dodd-Frank that allows the FDIC to treat similarly-situated creditors differently if this will maximize the value of the firm's assets?[223] Assuming that Dodd-Frank does in fact contemplate that the FDIC can pick and choose among similarly-situated creditors,[224] it is not clear that this would constitute a violation of the "uniform laws" requirement. One can have a law that uniformly provides for dissimilar or even random treatment of similarly-situated claimants. An example might be a bankruptcy law providing that creditors will be selected for payment by lottery. We do not suggest that such a law would be desirable. Uniform treatment of similarly-situated creditors is unquestionably an important *policy* of the bankruptcy laws, since it critical in overcoming the competitive race among creditors to capture a limited pool of assets, which bankruptcy is designed to prevent.[225] Dodd-Frank, by giving the FDIC discretion to treat similarly-situated creditors differently, may stimulate a competitive race to influence federal regulators to favor one creditor over others. Nevertheless, deviation from sound bankruptcy principles does not necessarily equate to a violation of the uniformity requirement. In our view, "uniform Laws" means that one debtor cannot constitutionally be singled out for dissimilar treatment; but it is probably too much of a stretch to say the Constitution requires that all similarly-situated creditors must be treated alike.

B. First Amendment

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nondelegation doctrine. To be sure, decisions like *Fahey* have stressed that broad delegations are permissible in part because judicial review is available to hold the executive in check. As previously discussed, judicial review of the decision to seize a firm and put it into receivership is sharply limited under Dodd-Frank. Whether courts will continue to stress the need for judicial review, however, is unclear. See Thomas W. Merrill, Delegation and Judicial Review, 33 Harv. J. L & Pub. Pol'y 73 (2010).

[223] DFA, §210(b)(4).

[224] The statute in fact says that all claimants "that are similarly situated…shall be treated in a similar manner," subject to an exception where the FDIC determines that it is necessary to deviate from equality in order to maximize the value of estate assets. DFA, §210(b)(4). The government argues in *Big Spring* that the exceptions would apply only in narrow circumstances, such as where payment to utilities should be continued to keep the lights on. A narrowing construction to this effect would go a long way toward undermining the premise of the states' argument about dissimilar treatment of creditors. See Defendants' Motion to Dismiss the Second Amended Complaint, State National Bank of Big Spring v. Wolin, No. 1:12-cv-0132 (ESH) (filed Feb. 22, 2013) at 46-48.

[225] See, e.g., Thomas H. Jackson, Avoiding Powers in Bankruptcy, 36 Stan. L. Rev. 725, 758 (1984).

Dodd-Frank is also vulnerable to challenge because it contains a provision imposing stiff criminal penalties on persons who disclose truthful information about pending cases in an Article III judicial proceeding.[226] Of course, judicial proceedings are sometimes conducted in camera, as when a grand jury considers whether to bring a criminal indictment or the government seeks a warrant to search or arrest. And discovery materials or settlement agreements are sometime put under seal, as when the parties stipulate to a confidentiality agreement. But the idea that a defendant can be criminally punished for disclosing truthful facts about an adversarial judicial proceeding the government has brought against the defendant is without precedent.

One can readily imagine circumstances in which Dodd-Frank's statutory gag rule would raise serious First Amendment issues. Suppose a financial firm is notified that a petition has been filed to appoint a receiver to liquidate it under Title II. The firm believes that the petition has been filed because it is on an "enemies list" established by the President to punish firms that have not contributed to his re-election campaign. The firm further concludes that its only hope of salvation is to leak the information about the pending receivership to the press, in an effort to rally opposition to the move. Dodd-Frank seeks to deter such action by imposing criminal punishment of up to five years in prison for speaking out about what is happening.

A First Amendment test of Dodd-Frank's gag rule may never arise, because typically none of the parties to the proceeding to appoint a receiver will have an interest in disclosure. Other than the executive branch officials and the court personnel involved, only the officers and directors of the targeted firm will know about the proceeding, "and they are probably the last ones who would want the petition for a receivership to be disclosed."[227] This is no doubt true in a case where the firm is about to collapse and the government is acting in good faith. But the First Amendment, like other provisions of the Bill of Rights, was adopted on the assumption that the government will not always be operating in good faith. Obviously, Dodd-Frank's criminal penalties for disclosing truthful information about an OLA proceeding could only be challenged by someone who proposes to engage in conduct that would give rise to potential criminal liability.[228] The question is whether its constitutionality would be sustained in such a context.

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[226] DFA, § 202(a) (1)(C).

[227] Baird and Morrison, supra note 104 at 298.

[228] Clapper v. Amnesty International USA, No. 11-1025 (February 26, 2013), would appear to bar an anticipatory challenge to the gag rule by a creditor anxious to receive information about any petition to put a financial firm into receivership.

The government might attempt to argue that the gag rule is analogous to the rules that prohibit witnesses in grand jury proceedings from disclosing their testimony.[229] But grand jury proceedings are not a final determination of criminal liability. If the grand jury returns an indictment, the defendant is free at trial to call relevant witnesses to testify in open court in an effort to be exonerated.[230] In contrast, once a petition to appoint a receiver is approved under Dodd-Frank's OLA, a receivership commences that inevitably leads to mandatory liquidation of the targeted firm, as well as other irrevocable consequences such as the elimination of stockholder equity and the dismissal of all directors. In this sense, the Dodd-Frank gag rule is more analogous to an order closing a public trial, something highly disfavored under the First Amendment. [231]

The government may also seek to analogize the gag rule to the rules of secrecy associated with proceedings to obtain a search warrant, confidentiality agreements, civil commitment proceedings, or juvenile trials. But these secrecy rules can be explained on grounds of consent. Government employees involved in judicial proceedings for issuing warrants or orders for national security wiretaps can be prohibited from disclosing what goes on in these proceedings, because they have explicitly or implicitly agreed to these constraints by accepting public employment.[232] Confidentiality agreements are also based on consent, as where parties agree not to disclose the existence of a civil action or (more commonly) the settlement of a civil action.[233] Civil commitment and juvenile justice proceedings are also often confidential. But here too, typically, the party against whom the action is directed fully supports maintaining the confidentiality of the proceeding. Given that government employees and parties to lawsuits can consent to secrecy, Dodd-Frank's gag rule is presumably justifiable as applied to Treasury Department or FDIC officials, as well as court personnel, because these officials have consented

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[229] See Douglas Oil Co. v. Petrol Stops Northwest, 441 U.S. 211, 222 (1979); United States v. Procter & Gamble Co., 356 U.S. 677 (1958).

[230] Cf. Butterworth v. Smith, 494 U.S. 624 (1990) (holding that publication of grand jury testimony may not be prohibited once the term of the grand jury is over).

[231] In the context of criminal trials of adults, the Court has held that even if the prosecutor and the defendant agree to make the proceedings confidential, the First Amendment allows interested third parties (such as the press) to object on First Amendment grounds. See Press-Enter. Co. v. Superior Court, 464 U.S. 501 (1984); Richmond Newspapers, Inc. v. Virginia, 448 U.S. 555 (1980).

[232] See Snepp v. U.S. 444 U.S. 507, 510 n.3 (1980) (holding that the requirement that Snepp get the CIA's approval of any memoir he might write prior to its publication was not an unconstitutional restraint on free speech as Snepp had voluntarily signed an agreement to that effect both upon the commencement of his employment with the CIA and just prior to his departure).

[233] Seattle Times Co. v. Rhinehart, 467 U.S. 20 (1984) (holding protective order prohibiting a newspaper from publishing information which it had obtained through discovery procedures did not offend the First Amendment).

to preserve confidential information that pertains to their public functions.[234] But threatening officers or directors of a targeted firm with criminal punishment for disclosing truthful information about a court proceeding in which they have been involuntarily drawn is different. When the government brings a civil action against a party, and that party seeks to disclose truthful information about the proceeding, there is little precedent suggesting that the party can be criminally punished for doing so.

Perhaps the closest analogy is provided by National Security Letters (NSLs) authorized by the Patriot Act. The Act allows the government to issue NSLs requesting records from wire or electronic communications service providers as part of an investigation of potential terrorist activity, and prohibits the service provider from disclosing that such information has been sought.[235] The Second Circuit has held that there can be a compelling governmental interest in preserving the confidentiality of NSLs. [236] But the court also concluded that relevant First Amendment authority requires that any such restraint on speech must be narrowly tailored to serve the government's interest in confidentiality. The court further concluded that the government must bear the burden of proving, in each case, that there is good reason to believe that disclosure of a NSL would jeopardize a national security investigation.[237]

There are nevertheless significant differences between NSLs and Dodd-Frank's nondisclosure requirement. One question is whether the government interest in preserving the confidentiality of an OLA petition is as compelling as that in preserving the secrecy of an investigation of potential terrorists. If one assumes premature disclosure of an OLA proceeding could trigger a financial panic, the answer is presumably yes. A financial panic would be devastating to national economy, inflicting damage of a different sort than a terrorist attack, but nevertheless something equally to be avoided if at all possible. Another question is whether a case-specific justification of the need for secrecy is required by the First Amendment, as the Second Circuit held in the context of an NSL.[238] Dodd-Frank includes no requirement of a government demonstration of the need for confidentiality in each case in which an OLA proceedings is initiated. Congress apparently assumed that confidentiality would always be required in order to prevent a financial crisis analogous to a run on the bank. But it is not clear this assumption is necessarily correct. One can imagine a case in which a systemically significant nonbank financial firm is already known to be insolvent before an OLA proceeding is

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[234] See United States v. National Employees Union, 513 U.S. 454 (1955).

[235] 18 U.S.C. § 2709 (2000).

[236] John Doe, Inc. v. Mukasey, 549 F.3d 861, 878 (2d Cir. 2009).

[237] Id. at 883.

[238] John Doe, Inc., supra, 549 F.3d at 878-881.

commenced, in which case the news would already have been absorbed by the market. It is not at all clear why the gag rule is necessary in such a situation. So perhaps an individualized justification of secrecy is required in the OLA context too.

There is a more fundamental reason why Dodd-Frank's gag rule fails the narrow tailoring requirement. This is because the government had the option of structuring OLA like an ordinary bank receivership, in which plenary judicial review of the decision to appoint a receiver would occur ex post rather than ex ante. Putting the judicial hearing after the receiver is appointed eliminates any need for secrecy, as well as any need for a rush to judgment and the other problems previously considered in connection with a due process or Article III challenge. Once again, we see that the Senate's amendment injecting a federal district court into the process of appointing a receiver was an unforced error generating constitutional problems that could readily have been avoided.

V. Takings Issues

We conclude with some takings issues. Title II contains a number of provisions that conceivably could give rise to takings claims. It is difficult to speak with any certitude about how these might be resolved. Short of outright seizure or destruction of a recognized property right by the government, takings claims are resolved under an ad hoc regime that depends critically on the specific facts presented.[239] We will briefly note some situations that seem especially likely to generate future takings claims, and then offer somewhat more complete analysis of the largest takings issue looming on the horizon: impairment of secured creditor claims in order to avoid taxpayer-funded bailouts.

Tracking the language of the Constitution,[240] takings claims can potentially present four issues: Does the claimant have an interest in "private property"? Has the government "taken" this property? If so, was the taking for a "public use"? And finally, has the government made adequate provision to provide "just compensation" for the taking?

Of these four issues, the "public use" question is probably the least likely to be contested. Most would agree that seizing a firm to prevent or forestall a financial crisis, which is the premise for exercising Title II authority, is a legitimate public use.[241] To be sure, just because

[239] Penn Central Transp. Co. v. New York, 438 U.S. 104, 124 (1978).

[240] "Nor shall private property be taken for public use without just compensation." U.S. CONST. amend. V. For an overview of these issues, see DAVID A. DANA AND THOMAS W. MERRILL, PROPERTY: TAKINGS (2002).

[241] The Supreme Court has defined "public" use broadly to include public benefit or advantage. Kelo v. City of New London, 545 U.S. 469 (20050; see DANA AND MERRILL supra, at 191-209.

the Title II process as a whole satisfies the public use requirement, it does not necessarily follow that every seizure of property undertaken pursuant to a Title II proceeding is also for a public use. Still, assuming there is some nexus between the seizure and the purposes of Title II, a public use challenge will likely fail.[242] The "property," "taking," and "just compensation" issues are more likely to arise, if and when OLA is used and one or more aggrieved stakeholders elects to pursue a takings claim.

A. Some Possible Takings Claims

1. *Assessments.* Given its desire to avoid anything resembling a bailout of failed financial firms, Dodd-Frank provides that if Treasury funds are needed to support a financial firm during the resolution process, these must be repaid. The first source of repayment is the firm's stakeholders – shareholders are wiped out and unsecured creditors will have their claims reduced, if necessary to zero. If this still leaves a debt to the Treasury, then the Act provides that the FDIC can impose "assessments" on a broad list of financial institutions.[243] Those eligible to be tapped include any bank holding company with at least $50 billion in assets, any nonbank financial company subject to systemic risk oversight under Title I, and any other "financial company" with assets of at least $50 billion.[244]

Financial firms that are assessed to pay for the resolution of some other insolvent financial firm may claim that this kind of monetary exaction constitutes an unconstitutional taking of property. Although the principle has not been enforced by the Supreme Court for many decades, there is older authority holding that special assessments disproportionate to any benefits conferred are takings.[245] Today, a threshold question would be whether the imposition of a general monetary liability of this nature can ever be challenged as a taking. In *Eastern Enterprises v. Apfel*,[246] five Justices joining separate opinions thought not; in their view the

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[242] Whether a taking is for a public use must ordinarily be resolved before a taking occurs, since if the taking lacks a public use, it should be enjoined. See D. Zackary Hudson, *Eminent Domain Due Process*, 119 YALE L. J. 1280 (2010). Dodd-Frank's OLA provisions offer no clear way to raise the public use issue before the seizure of a financial firm occurs. If a claimant has a legitimate public use objection, this would be an additional constitutional reason to condemn the statute.

[243] DFA, § 210(o)(1)(B).

[244] DFA, § 210(o)(1)(A).

[245] Village of Norwood v. Baker, 172 U.S. 269 (1898); cf. Louisville & Nashville RR. V. Barber Asphalt Paving Co., 197 U.S. 430 (1905) (permitting assessments based on general criteria like frontage footing); see generally Robert C. Ellickson, *Suburban Growth Controls*, 86 YALE L. J. 385, 469-73 (1977).

[246] 524 U.S. 498 (1998); see id. at 540-42 (Kennedy, J. concurring in the judgment and dissenting in part); id. at 554-55 (Breyer, J. dissenting). For a defense of the discrete assets limitation, see Thomas W. Merrill, The Landscape of Constitutional Property, 86 Va. L. Rev. 885, 974-78 (2000).

Takings Clause applies only to interferences with discrete assets. If the Clause does apply, the government would likely argue that liability for such assessments is analogous to a special tax to help redress a problem unique to the industry being taxed, such as a tax on chemical feedstocks to pay for hazardous waste cleanups.[247] Financial firms that object to paying assessments would likely stress the unfairness of forcing them to fund a general public good – avoidance of financial crisis -- when there is no required finding that they were at fault or even causally connected to behavior that gave rise to the crisis. Whether this would succeed if framed as a takings claim is doubtful but not impossible.[248]

2. *Executive Pay Clawbacks.* Dodd-Frank requires the removal of officers of the financial firm if they are found to have been "responsible" for the company's financial failure. It also permits the FDIC to claw back any compensation they received during the two years prior to the start of the receivership.[249] The clawback is not limited to "excessive" compensation, nor is there any statutory requirement of specific misconduct on the part of the officer that produced inflated compensation. To the contrary, the statute instructs the FDIC to weigh the "financial and deterrent benefits" of a clawback against "the cost of executing the recovery."[250] This appears to be close to mandating a clawback whenever it would be cost effective to do so, without regard to the culpability of the officer or the excessive size of the compensation package.

Executives subject to such clawbacks might argue that the statute goes far beyond traditional notions of avoidable preferences and fraudulent conveyances in bankruptcy,[251]and constitutes nothing more than an attempt to expropriate their wealth in order to promote the general good of achieving financial stability. The government would likely argue that Dodd-Frank's executive clawbacks are consistent with recent clawback provisions in the Sarbanes-Oxley Act and the TARP legislation[252] and are broadly equitable and fair. The outcome, again,

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[247] An earlier version of the Dodd-Frank Act provided for the creation of such a fund, but this was deleted by the Senate in order to reduce the perception that the statute contemplated "bailouts." CERCLA or Superfund, as originally enacted in 1980, provided for a tax on chemical companies, see 42 U.S.C. 9507(b)(1); this tax, in turn, supplied a fund for cleanup of hazardous waste sites. 42 U.S.C. 9611. The tax expired in 1995 and has not been reauthorized.

[248] For an analogous argument, albeit in a dissenting opinion, see Pennell v. City of San Jose, 485 U.S. 1, 15-16 (1988) (Scalia, J., concurring in part and dissenting in part) (arguing that it is a taking to force landlords to accept reduced rents based on "tenant hardship" for which they bear no responsibility).

[249] DFA, § 210(s)(1).

[250] DFA, § 210(s)(2).

[251] See 11 U.S.C § 547(b)(4)(B) (allowing the trustee to avoid transfers made by the debtor to insiders with one year or less of the debtor filing for bankruptcy); but also see § 547(c) (prohibiting a trustee from avoiding a transfer that was made to any creditor in exchange for new, contemporaneous value given to the debtor).

[252] See Spencer C. Barasch & Sara J. Chesnut, Controversial Uses of the "Clawback" Remedy in the Current Financial Crisis, 72 Tex. B. J. 922 (2009).

is difficult to handicap, and might turn on what a court concludes is the relevant baseline for establishing legitimate expectations about the vulnerability of executives to salary clawbacks. If baseline is that established by the Bankruptcy Code, executive would have a chance of prevailing; if more recent legislation is deemed to the relevant baseline, their chances would diminish.

3. *Revival of Barred Actions.* Dodd-Frank contains an unusual provision allowing the FDIC as receiver to bring tort claims on behalf of the entity in receivership even though the statute of limitations has expired.[253] The purpose is obviously to allow the FDIC to recover funds from former managers and other miscreants perceived to have caused the covered financial firm to experience financial losses. The covered claims include "fraud, intentional misconduct resulting in unjust enrichment, or intentional misconduct resulting in a substantial loss to the covered financial company." Fraud and unjust enrichment are well established common-law causes of action; "intentional misconduct resulting in substantial loss" is not, so the exact scope of this provision is unclear. The statute of limitations must have expired within 5 years of the appointment of the FDIC as receiver in order for the claim to be eligible for revival.

Persons targeted in these cases may claim that reviving a cause of action for damages previously barred by the statute of limitations represents a taking of property. The Supreme Court has sometimes said that reviving actions barred by the statute of limitations would be a taking,[254] but more often has said it is not.[255] Clearly, reviving liabilities previously barred by the statute of limitations interferes with the repose these statutes are designed to promote. Not surprisingly, perhaps, legislative revivals of liability have been declared unconstitutional under provisions other than the Takings Clause.[256] Thus, it is difficult to predict with any confidence how such an action would ultimately be assessed today under a takings challenge.

B. Impairment of Security Interests

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[253] DFA, § 210(a)(10)(C).

[254] William Danzer & Co., Inc. v. Gulf & Ship Island R. Co., 268 U.S. 633 (1925).

[255] Chase Securities Corp. v. Donaldson, 325 U.S. 304 (1945); Campbell v. Holt, 115 U.S. 620 (1885). In the latter case the Court distinguished between actions to recover real or personal property, where the passage of the statute of limitations confers a title to property by adverse possession or prescription, and actions to recover of a debt, where the statute merely bars enforcement in court.

[256] See Stogner v. California, 539 U.S. 607 (2003) (holding that once criminal prosecution is barred by statute of limitations, revival of action constitutes an ex post facto law); Plaut v. Spendthrift Farm, Inc., 514 U.S. 211, 217-19 (1995) (holding that once action has been dismissed by federal court as barred by statute of limitations, enactment of a statute that adopts a longer statute of limitations and seeks to reopen judgments violates Article III).

The most significant takings issues potentially implicated by Dodd-Frank involve security interests.[257] In the quest to find sources of funding other than tax revenues to prop up firms undergoing resolution, the House bill, H.R. 4173, provided that certain secured creditors would be required to take a haircut of up to 10 percent of the value of their security interest if "the amounts realized from the dissolution are insufficient to satisfy completely any amounts owed to the United States…."[258] No such provision was included in the Senate bills or the version of the statute as enacted. In a tip of the hat to the House, the final version of the Act did include a section requiring the Financial Stability Oversight Council to conduct a study as to whether secured creditors should be required to take a haircut in future OLA proceedings.[259] The study, which was completed in July 2011, recommended against amending the law to permit impairment of security interests, largely on the ground that the other powers given by the Act are sufficient to avoid future taxpayer bailouts without going after secured creditors.[260] Given the Council's advice, a revision of the law permitting impairment of security interests appears unlikely for the moment. Nevertheless, there is a very real possibility that Congress will demand the impairment of secured creditor rights in some future financial crisis, in the interest of avoiding taxpayer liability.[261]

A security interest is essentially a contingent property right held by a lender in specific assets owned by the borrower.[262] In terms of conventional property forms, security interests are

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[257] Unsecured claims are commonly reduced or disallowed in bankruptcy and other insolvency proceedings. A state law that retroactively impaired unsecured creditor rights could give rise to a claim under the Contracts Clause. See Ogden v. Saunders, 25 U.S 213 (1827). But for purposes of the Takings Clause, unsecured claims are regarded as contract rights, not property rights, and hence impairment by the federal government through bankruptcy-proceedings does not give rise to any issue under the Takings Clause. As previously noted, unsecured claims *are* regarded as property for due process purposes. Tulsa Professional Collection Services, Inc. v. Pope, 485 U.S. 478, 485 (1988).

[258] H.R. 4173, § 1609(a)(4)(D)(iv). The interests covered where short term financial contracts secured by securities other than instruments of the United States or interests in land.

[259] DFA, § 215.

[260] Financial Stability Oversight Council, Report to the Congress on Secured Creditor Haircuts (July 2011) at http://www.treasury.gov/initiatives/Documents/report%20to%20congress%20on%20secured%20creditor%20haircuts.pdf.

[261] Recent academic commentary has argued that secured creditors have insufficient incentives to monitor distressed firms, and that eliminating the absolute priority rule for secured creditors would result in better monitoring. See Douglas G. Baird, Security Interests Reconsidered, 80 Va. L. Rev. 2249, 2259 (1994). An earlier generation of scholars worried that secured creditors were likely to leave insufficient assets in a bankrupt enterprise to satisfy the claims of nonadjusting creditors like torts claimants. See, e.g., Lucian A. Bebchuk & Jesse M. Fried, The Uneasy Case for the Priority of Secured Claims in Bankruptcy, 105 Yale L. J. 857 (1996). Both types of arguments presuppose that security interests are not constitutionally protected by the Takings Clause.

[262] See Baird supra at 2257 ("Security interests under Anglo-American law have always been tied to particular assets. A creditor acquired an interest in a particular piece of real and personal property and looked to it first to obtain repayment.")

analogous to executory interests: They are a nonpossessory future interest that may or may not vest, depending on the happening of a future contingency, namely, the borrower's default on the loan. If the loan is repaid in a timely manner, the security interest is released. If the loan is not repaid in a timely manner, this gives the security interest holder the right to seize or compel the sale of the asset in order to generate funds to repay the loan.

Under the Bankruptcy Code, security interests are implicitly treated like property rights that belong to the secured creditor, although the Code studiously avoids labeling them "property." In a liquidation proceeding, a secured creditor is entitled to the full amount of its secured claim.[263] The trustee in bankruptcy can either sell the property subject to the security interest,[264] in which case the security interest follows the property, or can sell the property free of the security interest,[265] with the proceeds of the sale being used to satisfy the secured debt.[266] If the value of the asset is equal to or worth less than the unpaid balance due on the loan, the trustee can abandon the property to the security holder.[267] Security interests are subject to the automatic stay in bankruptcy, which can potentially impair the value of the security.[268] The Code requires that the trustee provide "adequate protection" to secured lenders to minimize losses due to the stay.[269]

Things are more complicated in a reorganization proceeding. Here, the bankruptcy trustee (or debtor in possession) can with the approval of the bankruptcy court decide that the specific asset in which a creditor holds a security interest is necessary to the success of the reorganized firm.[270] In this event, the court can decide to keep the asset for the use of the reorganized firm. If it does so, however, it must perform a valuation of the asset and give the secured creditor a substitute for its property right – a "secured claim to the extent of the value of such creditor's interest."[271] The Code again requires that secured creditors given these substitute rights must be given "adequate protection" that they will receive an "indubitable

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[263] Dewsnup v. Timm, 502 U.S. 410, 417 (1992).

[264] 11 U.S.C. § 363(b) & (c).

[265] Id. at § 363(f).

[266] Id. at § 363(j).

[267] Id. at § 554.

[268] Id. at § 362.

[269] Id. at § 363(e).

[270] Id. at § 1123.

[271] 11 U.S.C. § 506(a).

equivalent" to the value of the property in which they previously held a security interest.[272] By allowing the bankruptcy court to substitute other rights of equivalent financial value for the security interest, the Code treats security interests as if they are fungible assets equivalent to money, and hence as something the court is free to exchange for money.

As enacted, the Dodd-Frank Act follows the Bankruptcy Code in recognizing the distinctive status of security interests, and in particular in recognizing that they are entitled to adequate protection without regard to the impact this has on other creditors or on larger objectives such as preventing the collapse of a systemically significant firm.[273] As in the case of the Bankruptcy Code, there is no acknowledgment in Dodd-Frank that security interests are property or that the abrogation of security interests in order to enlarge the pot of assets available for other worthy ends might raise constitutional questions.

Notwithstanding its general posture in favor of preserving security interests, Dodd-Frank Title II deviates in certain respects from the way security interests are treated in bankruptcy. The clearest example concerns setoffs, as when a creditor holds funds of an insolvent debtor which the creditor then seeks to take as full or partial satisfaction of an unpaid claim. The Bankruptcy Code treats setoffs as a type of secured claim; Dodd-Frank does not.[274] Thus, it is foreseeable that some creditor denied treatment of a setoff as a secured claim will argue that this is a taking requiring the government to make up the difference by paying just compensation. The question is whether this type of deviation from the treatment of security interests in bankruptcy, or other reductions in secured creditor rights in the future in response to demands for alternative sources of funding of resolutions of systemically significant firms, could be challenged as a taking.

Under the relevant decisions of the Supreme Court, it is reasonably clear that security interests are "property" protected by the Takings Clause. The issue arose in a series of Depression-era cases under the Frazier-Lemke Act, which allowed farmers to obtain a moratorium on foreclosure and to convert mortgaged farm property into a temporary leasehold.[275] The Court stated unequivocally that mortgages are property and that the Takings Clause applies.[276] It then offered shifting judgments about whether the moratorium and

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[272] 11 U.S.C. §§ 362(d)(1); 361; 1129(b)(2)(A) .

[273] DFA, § 210(a)(3)(B) ("The receiver shall allow any claim… which is proved to the satisfaction of the receiver.")

[274] DFA, § 210(a)(7)(B). The Bankruptcy Code does not grant setoff rights per se; creditors' setoff rights are governed by state law. See Citizens Bank v. Strumpf, 516 U.S. 16 (1995). Section 553 of the Bankruptcy Code does however acknowledge that a creditor has the right of setoff under state law and preserves setoff rights. See 11 U.S.C. § 553. Section 506(a) treats valid setoff rights as a secured claim. Id. at § 506(a).

[275] 11 U.S.C 203(s) (1934).

[276] Louisville Joint Stock Land Bank v. Radford, 295 U.S. 555, 601 - 602 (1935).

conversion was a taking. It struck down the initial version of the Act,[277] but upheld a modified version two years later that shortened the moratorium period.[278] In another widely cited decision, *Armstrong v. United States*, [279] the Court again stated unequivocally that a materialmen's lien is property protected by the Takings Clause. It held that when the United States seized property subject to such a lien with the result that the lien was completely destroyed, this was a taking. Most recently, the Court addressed a provision of the Bankruptcy Code that exempted certain household furnishings from judgment liens. The Court held that the exemption should apply only prospectively and not to liens in existence when the Code was adopted. Relying on its decisions holding mortgages and materialmen's liens to be property, the Court reasoned that judgment liens are "property" and that the complete abrogation of a pre-existing lien by statute would raise "substantial doubt" under the Takings Clause.[280]

Although the Court's decisions collectively establish that security interests are "property" for takings clause purposes, they nevertheless leave many questions unanswered. One question is whether the status of security interests as property is subject to prospective modification by legislation or regulatory pronouncement.[281] There is a strong suggestion in *Security Industrial Bank*, the most recent decision, that prospective override of security interests would not be a taking.[282] This might mean, for example, that creditors who obtain setoff rights after the enactment of Dodd-Frank Title II cannot claim that the failure to treat these rights as property for bankruptcy purposes is a taking, because Title II announced to the world that henceforth they would not be treated as such. Setoff rights are close enough to the line between property and contract rights (which clearly are subject to compromise or even disallowance in bankruptcy) that this kind of re-classification may be permissible. It is less clear whether an announcement by Congress (or a federal agency) modifying the absolute priority given to

[277] *Id.*

[278] Wright v. Vinton Branch of the Mountain Trust Bank, 300 U.S. 440 (1937).

[279] 364 U.S. 40 (1960).

[280] United States v. Security Indus. Bank, 459 U.S. 70 (1982).

[281] Compare James Stevens 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 (1983) (arguing that Congress has complete discretion to modify the priority or other treatment of secured creditor rights under the Bankruptcy Clause) with Julia Patterson Forrester, *Bankruptcy Takings*, 51 FLA. L. REV. 851 (1999) (arguing that prospective modification of secured creditor rights that go beyond settled background principles of property law can give rise to takings liability).

[282] The Court specifically reserved the issue whether the Act would apply to liens established after the Act was passed but before it became effective. See *Security Industrial Bank*, 459 U.S. at 82 n.11. But the Court did not reserve the question whether a judgment lien established *after* the Act became fully effective was also susceptible to a takings challenge. Thus, the Court implicitly assumed the provision could be applied in a fully prospective fashion.

security interests in bankruptcy would be enough to immunize the government from any takings claims arising in security interests created thereafter. At least with respect to interests in land, the Court has been reluctant to regard every newly-legislated or regulated land use restriction as an automatic qualification of property, such that persons who acquire restricted property in the future are automatically barred by the restriction.[283] The Court has acknowledged that property rights are qualified by "background principles" of property law, such as the understanding that landowners can be barred from engaging in uses that create nuisances.[284] Apparently, however, only longstanding limitations such as those recognized at common law count as relevant "background principles." This leaves considerable uncertainty about how the Court would respond to a law that prospectively modified the absolute priority of security interests. Delays on foreclosure have been around a long time and presumably qualify as "background principles;"[285] subordination of security interests to the need to avoid taxpayer bailouts might be regarded as a novelty that does not so qualify.

Another question is how haircuts of security interests or other modifications in the rights of security interest holders should be analyzed in terms of total or partial takings. *Armstrong* holds that the total destruction of a security interest is a taking,[286] and this tracks the analysis of *Lucas v. South Carolina Coastal Council*[287] in terms of real estate. But if Congress or the FDIC as receiver shaves ten percent off the principal value of a security interest in order to reimburse the federal treasury for temporary financing, would this be regarded a total taking of ten percent of the security or only a partial taking of ten percent of the security? In the case of land, shaving ten percent off the existing acreage is clearly a total taking of the ten percent.[288] But imposing a use regulation on the land that reduces its value by ten percent is only a partial taking, and is typically not compensable. This might suggest, by analogy, that imposing a ten percent haircut on secured interest holders would be a taking – especially if the purpose is to generate additional revenue for the government. But the matter is obviously debatable.

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[283] See, e.g., Lucas, supra (limiting background principles to common law); Palazzollo v. Rhode Island, 533 U.S. 606 (2001) (declining to recognize a per se rule that land use regulations in effect at the time of purchase qualify property rights); see also Philips v. Washington Legal Foundation, 524 U.S. 156, 163 (1998) (holding that regulatory requirement imposed on client funds held in trust by lawyers did not qualify common law understanding that interest follows principal).

[284] Lucas v. South Carolina Coastal Council, 505 U.S. 1003 (1992).

[285] See Forrester, supra, at 881-84.

[286] Armstrong, supra, 364 U.S. 40 (1960).

[287] 505 U.S. 1003 (1992) (holding regulation that destroys all economically beneficial value of real property is a taking unless it tracks the common law of nuisance in the relevant jurisdiction).

[288] See Loretto v. Teleprompter Manhattan CATV Corp., 458 U.S. 419 (1982) (regulation that permanently transfers control over a small cable box on the roof of a building is categorically a taking).

Yet more questions are presented about what constitutes just compensation when security interests are impaired. For example, must compensation be paid for the time value of money when recovery of the equivalent value of secured interest is delayed? Under the Bankruptcy Code, the Court has held as a matter of statutory construction that value lost due to delay is not compensated.[289] But the matter might come out differently when framed as a takings claim under the Fifth Amendment. The ultimate valuation question is presented by the standard, borrowed from FDIC receivership law,[290] that a secured creditor is entitled to recover at least as much as would have been obtained in a liquidation.[291] This gives rise to a question of what assumption the FDIC (or a reviewing court) is to make about the state of the economy when such a hypothetical liquidation occurs. If Dodd-Frank's OLA only applies to "systemically significant" firms whose failure would lead to financial crisis, are we to assume that the economy is in a state of financial collapse?[292] Does this mean that even if impairment of security interests is a taking, no compensation would be owed?[293] Or to avoid undue speculation, should the FDIC (and the court) take evidence on what the liquidation value would be given state the economy is in when the valuation takes place, which, if Title II works as advertised, would not be a state of total collapse?

Conclusion

The constitutional questions presented by Dodd-Frank's orderly liquidation authority can be seen either as a dark portent of an inverted constitutional order, or as a set of relatively easily avoided mistakes caused by careless last-minute drafting.

The dark vision goes something like this. The U.S. Constitution, like American law more generally, is designed for a world in which the government is seen as a potential threat to private rights, but private rights are not individually significant enough to pose a threat to government or society more generally. The Constitution was not designed for a world in which some privately-owned firms are so "systemically significant" that special rules must be devised to allow the government to take them over and operate them if they take on too much risk and are in danger of collapse. In order to construct a world in which a central function of the government is to

[289] See United Savings Assn. of Texas v. Timbers of Inwood Forest Associates, Ltd., 484 U.S. 365 (1988) (holding that the Bankruptcy Code does not require compensation for the time value of a secured interest).

[290] See 12 U.S.C. § 1821(i) (providing that the maximum liability of the FDIC to a person having a claim against an institution is the amount the claimant would have received if the FDIC had liquidated the institution).

[291] DFA, § 210(d)(2), (3).

[292] Baird and Morrison, supra note 104 at 316.

[293] Cf. Brown v. Legal Foundation of Washington, 538 U.S. 216 (2003) (holding that a taking does not require compensation if the claimant would have received nothing in the absence of the taking).

protect society from firms that are too big to fail, while nevertheless permitting such firms to continue to exist, constitutional rules must be fundamentally adjusted. Conventional norms of due process, understandings about the proper functioning of courts, limits on the legislative power reflected in the Bankruptcy Clause, and even free speech rights must give way. Property rights must be dissolved into a general mass of claim-rights, subject to reallocation by the government in order to advance its perception of the requirements of the general welfare. If the Constitution is supposed to be a bulwark that protects us from government, is Dodd-Frank a foretaste of what to expect when the government becomes the handmaiden of a financial oligarchy?

A more benign vision would stress that most of the constitutional problems we have identified in Dodd-Frank stem from a single ill-considered decision by the Senate to abandon the judicial review provisions in the Administration's draft and the House bill in favor of a novel scheme calling for appointment of a receiver by an Article III court. The Administration draft and the House bill called for administrative appointment of a receiver, coupled with a right of plenary post-seizure judicial review. Had Congress adhered to this conception, which was borrowed from existing banking law, it would have eliminated any serious due process question, any Article III question, and any need for a gag rule that raises potential First Amendment questions. Constitutional issues arising under the Bankruptcy Clause's uniformity requirement could have been laid to rest by drafting a more rule-like and less discretionary conception what type of firm is eligible for resolution under Title II. And the various takings issues could have been avoided or made more manageable by tacking more closely to established common law and bankruptcy law precepts about clawbacks, assessments, and the status of security interests. These enumerated revisions are relatively minor in the larger scheme of things. They suggest that Dodd-Frank's orderly liquidation authority is not too big for the Constitution – if only Congress had given sufficient consideration to the Constitution when it drafted this complex and far-reaching legislation.