

REFLECTIONS ON THE GOLDEN SPIKE: A LOOK AT THE BANKRUPTCY REFORM ACT AND RAILROAD REORGANIZATION

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The Northern and Southern Railway has been operating at a loss for a number of years. Forseeing the inevitability of default on its next payroll, the company files a petition in bankruptcy, seeking court sponsored reorganization. After three or four years of continuous deficit operation and physical plant deterioration,¹ the bankruptcy court finally approves a reorganization plan: the claims of all mortgage bondholders are honored by giving them ten cents to the dollar in the form of common stock in the surviving corporation.² But the trains roll on and the company is able, though barely, to operate without further default. "We object," the creditors cry, "Our claims have been impaired and yet the railroad continues to operate just as before." "Hush," responds the court. "The public interest, that creditor first in line and most favored by our Congress, needs the rail service."

This note directs attention to a "takings" problem: the constitutional parameters within which the interests of the creditor in the bankrupt railroad's assets will be subordinated to the interests of the public in continued rail service. In particular, this note compares the historic plight of the railroad's creditor, as illustrated by the fictional scenario involving the Northern and Southern Railway, with his expected fare under the Bankruptcy Reform Act of 1978.³ In Section I, the "takings" problem will be developed through a discussion of the prior bankruptcy law and railroad reorganization cases arising thereunder. Sections II and III discuss the railroad's obligation to serve the public and the public's interest in being served, respectively. The former section reviews the conditions under which a common carrier railroad may terminate train service or abandon trackage; the latter section comments upon the federal experiments in nationalization—Amtrak and Com-rail—and reviews those cases striking the balance between creditor's

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1. *E.g.*, New Haven Inclusion Cases, 399 U.S. 392 (1970).

2. *E.g.*, Reconstruction Fin. Corp. v. Denver & R.G.W.R.R., 328 U.S. 495 (1946).

3. Bankruptcy Reform Act of 1978, 11 U.S.C. §§ 101-151326 (1979) [hereinafter cited as Reform Act]. In order to clarify citation, prior bankruptcy statutes will be cited to the United States Code with a 1976 date and their amendment will be noted.

rights and the obligation of the carrier to continue public service. Section IV outlines the pertinent reorganization reform of the 1978 Reform Act and examines the competing House and Senate bills. This note concludes that the Bankruptcy Reform Act of 1978 perpetuates by statute past judicial assessment of the proper balance between public and private interests in railroad reorganization while at the same time providing relief to the insolvent carrier's creditors.

I. The Framework of the Bankruptcy Law

Article I, section 8, of the United States Constitution explicitly charges Congress with the responsibility for a uniform and rational bankruptcy law.⁴ The Fifth Amendment also provides that there shall be no taking of private property for public use without just compensation.⁵ Normally, there is no conflict between the operation of the bankruptcy law upon the estate of an insolvent debtor and the Fifth Amendment prohibition of uncompensated takings of private property for public use; the debtor's property is simply distributed among his creditors according to a scheme which gives some claims priority over others and treats some debts as non-dischargeable.⁶

Under its authority over the law of bankruptcy, Congress has also enacted legislation authorizing and guiding business reorganization.⁷ If a business is insolvent or unable to make timely creditor payments, but nevertheless is a potentially profitable firm, the bankruptcy law provides the business with an opportunity to restructure its operations and debt, free from the burden of the creditors' claims.⁸ But if the reorganization does not meet with the approval of a majority of materially affected creditors, then the firm faces normal bankruptcy proceedings.⁹

For a number of reasons, railroad reorganization has always been treated separately under the bankruptcy acts.¹⁰ Other business reorganizations are the subject of a separate and distinct statutory scheme. The principal rationale is that every railroad, whether intrastate or interstate in scope, is engaged in interstate commerce, the protection and regulation of which is a responsibility charged by Congress to the Interstate Commerce Commission (ICC) under the authority granted by the

4. U.S. CONST. art. I, § 8, cl. 4 ("To establish . . . uniform Laws on the subject of Bankruptcies throughout the United States.").

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

6. 11 U.S.C. §§ 35, 93 (1976) (amended 1978); Reform Act, *supra* note 3, §§ 507, 523.

7. 11 U.S.C. §§ 501-799 (1976) (amended 1978); Reform Act, *supra* note 3, §§ 1101-74.

8. 11 U.S.C. §§ 714, 723 (1976) (amended 1978); Reform Act, *supra* note 3, §§ 301, 362.

9. 11 U.S.C. §§ 761-62 (1976) (amended 1978); Reform Act, *supra* note 3, § 1129.

10. 11 U.S.C. § 205 (1976) (amended 1978); Reform Act, *supra* note 3, §§ 1161-74.

Constitution's commerce clause.¹¹ The public is included in the reorganization process through its representative, the ICC.¹² A second reason that railroad reorganization is the subject of separate statutory treatment is that railroads are already subject to extensive ICC regulation,¹³ the purpose of which is to effect a rational interstate transportation system that is fair to both shipper and carrier, regardless of region. By requiring the railroad in bankruptcy to continue to comply with various ICC regulations and procedures, including continued public service, the "rationality" of the national transportation system is preserved.

Prior to the Bankruptcy Reform Act of 1978 the interests of the public entered the reorganization process by two means. First, each class of creditors of both railroads and other corporate business was required to accept or reject the proposed reorganization plan.¹⁴ However, in the case of a railroad's reorganization, the bankruptcy court could approve a plan despite its rejection by any class of creditors, provided that the court found that the plan "makes adequate provision for fair and equitable treatment for the interests or claims of those rejecting it [and] that such rejection is not reasonably justified in the light of the respective rights and interests of those rejecting it. . . ."¹⁵ Prior bankruptcy law also provided for the fair and equitable treatment of the claims by those creditors rejecting the reorganization plan of non-railroad businesses, but it included language requiring the "adequate protection" of the creditors' interests with *property*.¹⁶ In the determination of the "reasonableness" of the railroad creditor's rejection of a plan, the bankruptcy court would consider the public interest in continued rail service as well as any property satisfaction the creditor's claim.¹⁷

The second and more direct injection of the public interest was through the integral role played by the ICC in the creation and approval of a reorganization plan. Within six months after the filing of the petition in reorganization, or within the time limits established by any number of six-month extensions, the bankrupt railroad was required to file a reorganization plan with *both* the bankruptcy court and the ICC.¹⁸ Initially, the Commission would order hearings on the plan

11. 49 U.S.C.A. §§ 10501-05 (West 1979) (replacing 49 U.S.C. § 1 (1976)).

12. 11 U.S.C. § 205 (1976) (amended 1978); Reform Act, *supra* note 3, § 1164. The proper role of the ICC was a subject of considerable dispute in the drafting of the Reform Act. *See* section IV and particularly the text accompanying notes 169-82 *infra*.

13. *See* 49 C.F.R. §§ 1-1332.3 (1979).

14. 11 U.S.C. §§ 205(e), 575-576 (1976) (amended 1978).

15. *Id.* § 205(e) (amended 1978).

16. *Id.* § 616 (amended 1978).

17. *See, e.g.,* Reconstruction Fin. Corp. v. Denver & R.G.W.R.R., 328 U.S. 495, 535-36 (1946).

18. 11 U.S.C. § 205(d) (1976) (amended 1978).

and was required to approve a plan which "in its opinion . . . will be compatible with the public interest."¹⁹ Once certified by the ICC, the bankruptcy court would hold hearings to determine the fairness of the plan to the creditors.²⁰ Failing approval by the court, the plan would be sent back to the ICC, and the cycle begun again.²¹ Except with respect to public utilities, nowhere in the law of corporate reorganization did the public get so direct a voice in the restructuring of the business firm.²²

The ICC's active representation of the public's interest in a situation where there is already insufficient money to satisfy the claims of the railroad's creditors naturally raises the specter of an uncompensated taking of the creditor's estate for the benefit of the public.²³ This tension between creditors' rights and the public interest is well recognized by the courts charged with the responsibility of overseeing the reorganization process:

Underlying the provisions of Section 77 of the Bankruptcy Act is the principle that, in order to vindicate the public interest in continued rail service, the normal rights of creditors and investors may be held in suspension for a reasonable time in order to achieve reorganization, and upon reorganization may be drastically altered if necessary. Nevertheless, there are limits beyond which this public interest cannot be served without violating the constitutional prohibition against appropriation of private property for public use without just compensation.²⁴

Prior to the Reform Act, there were two contexts in which a takings problem arose. The first is typified by the facts of the *New Haven Inclusion Cases*.²⁵ On July 7, 1961 the New York, New Haven and Hartford Railroad filed a petition to enter bankruptcy reorganization.

19. *Id.*

20. *Id.* § 205(e) (1976) (amended 1978).

21. *Id.* One of the most frequent objections to this procedure is the excessive time delay. All the while the bankrupt is in reorganization, the creditor is without remedy, save for the sale of his claim at an extreme discount. *See, e.g.*, Wall St. J., Sept. 22, 1978, at 3, col. 2.

22. 11 U.S.C. §§ 577-578 (1976) (amended 1978).

23. *See, e.g.*, Reconstruction Fin. Corp. v. Denver & R.G.W.R.R., 328 U.S. 495, 535-36 (1946).

24. *In re Penn Central Transp. Co.*, 347 F. Supp. 1356, 1366 (E.D. Pa. 1972) (citing *New Haven Inclusion Cases*, 399 U.S. 392 (1970) and *Brooks-Scanlon Co. v. R.R. Comm'n*, 251 U.S. 396 (1920)). The court continued: "These limitations are measured both in term of the amount of erosion of the Debtor's estate which can be permitted to occur before impairing liquidation value, and in term of the length of time that is reasonable for assessing the ultimate prospects of achieving sufficient profitability to support a valid recapitalization of the enterprise. If there is sound support for a conclusion of ultimate profitability, interim erosion is less critical, except, of course, to the extent that it may require assurance of a greater degree of ultimate profitability because of the increase of priority debt which must be taken into account in the reorganization plan." 347 F. Supp. at 1366.

25. 399 U.S. 392 (1970).

Two years later it became apparent that the railroad would probably never become a profitable operation and the ICC attempted to force the New Haven to merge with another railroad.²⁶ The pending merger of the Pennsylvania and New York Central Railroads provided a convenient solution to the New Haven's problem. As a condition precedent to ICC approval of the Penn Central merger, the successor company was required to absorb the debt-ridden New Haven.²⁷

At issue in the *New Haven Inclusion Cases* was the price which the Penn Central Transportation Company would pay for the deteriorating assets of the New Haven railroad.²⁸ The district court approved an amount equal to the railroad's liquidation value as of December 31, 1966, almost five and a half years after the petition for reorganization was filed.²⁹ The mortgage bondholders, whose claims were already subordinate to back taxes and post-bankruptcy trustee certificates (used by the New Haven to finance operating losses), objected to a valuation that was some \$88 million less than the railroad's value when it entered reorganization.³⁰ Among other theories, the bondholders' suit alleged that the failure to compensate for the deterioration of the New Haven's assets in the 1961-1966 period was an uncompensated taking of their estate for public use.³¹ The Supreme Court acknowledged that the public interest could not compel a railroad to operate at a loss indefinitely,³² but it nevertheless held that since no bondholders had requested the liquidation of the New Haven prior to the 1966 valuation date, there could be no complaint as to the price.³³

The suggestion that the New Haven bondholders had no claim to a pre-1966 valuation of the railroad's assets solely because there had been no request for liquidation masks the Court's actual holding. This underlying concern became apparent in *In re Boston and Maine Corporation*.³⁴ In that case, the creditors *did* request the liquidation of the

26. *In re New York, N.H. & H.R.R.*, 304 F. Supp. 793, 800 (D. Conn. 1969). The district court stated, "By late 1963 it was clear . . . that only two courses were open: . . . the inclusion in a Penn Central merger or . . . liquidation. The former was obviously in the public interest and the latter was not." *Id.*

27. *Pennsylvania R.R.—Merger—New York Cent. R.R.*, 327 I.C.C. 475, 522-27 (1966). For a general discussion of the problems created by the inclusion of the unprofitable New Haven into an already financially weak Penn Central, see R. SOBEL *THE FALLEN COLLOSSUS*, ch. XI (1977).

28. 399 U.S. at 399.

29. *See In re New York, N.H. & H.R.R.*, 289 F. Supp. 451, 454 (D. Conn. 1968).

30. *Id.*

31. 399 U.S. at 489-95.

32. *Id.* at 491-92. *See Brooks-Scanlon Co. v. R.R. Comm'n*, 251 U.S. 396 (1920); *Railroad Comm'n v. Eastern Tex. R.R.*, 264 U.S. 79 (1924).

33. 399 U.S. at 493. For a highly critical analysis of this decision, see Note, *Takings and the Public Interest in Railroad Reorganization*, 82 *YALE L.J.* 1004 (1973).

34. 484 F.2d 369 (1973).

railroad, but the appellate court refused to take issue with the district court's approval of the bankruptcy trustee's authorization of capital expenditures over the objections of the creditors. "It has long been established," the appellate court stated, "that secured creditors may be required to defer realizing on their security for a reasonable time to permit the trustees to make efforts to reorganize the railroad."³⁵ Thus, while the court and the ICC search for a plan that accords with the public interest, the cost of delay in the slow reorganization process is constitutionally chargeable to the creditor's account.

The second occasion giving rise to the takings problem occurred when a reorganization plan had been approved and its rejection by a materially and adversely affected class of creditors was held unreasonable. Such a situation arose in *Reconstruction Finance Co. v. Denver & Rio Grande Western R.R.*,³⁶ where nearly eighty percent of the general mortgage bondholders rejected a reorganization plan under which they would receive ten cents to the dollar in stock in the reorganized company as compensation for their claims.³⁷ The Supreme Court, reversing an appellate court finding that the rejection by the bondholders was reasonable, stated:

These [creditors] cannot be called upon to sacrifice their property so that a depression-proof railroad system might be created. But they invested their capital in a public utility that does owe an obligation to the public. . . . [B]y their entry into a railroad enterprise, [they] assumed the risk that in any depression or any reorganization the interests of the public would be considered as well as theirs.³⁸

The Court did not indicate if, how, or to what extent, the rail investor is to be compensated for such assumed risk. Nor did it indicate what effect this unique form of bankruptcy risk would have on the creditworthiness and health of the railroad industry.

Whether it be the delay of the reorganization process or the treatment under the reorganization plan that causes an impairment of the creditor's estate, the argument justifying such impairment proceeds from the dual premises that (1) the public has an interest in continued rail service and (2) the carrier has an obligation to provide such service to the conclusion that the railroad's creditors may be required to bear the cost of this service. The next two sections will explore the railroad's obligation to serve the public and the public's interest in being served.

35. *Id.* at 374.

36. 328 U.S. 495 (1948).

37. *Id.* at 502.

38. *Id.* at 535-36.

II. The Obligation to Serve the Public

The obligation placed upon the railroad to serve the public derives from its historical role. The railroad industry, from the foundation of the original Baltimore and Ohio Railroad in 1826 to the semi-public Consolidated Rail Corporation in 1975, has been both sponsored and regulated by government.³⁹ Many railroads, most notably the transcontinentals, have received grants of land as incentive to expand their lines.⁴⁰ Most railroads have received only limited monopoly status and authority to exercise eminent domain in order to create rights-of-way.⁴¹ In exchange for this sponsorship, the railroads were obligated to serve the public along their lines.⁴² Government regulation of this service quickly followed the railroad's last spike, first through the establishment of state commissions and then with the creation of the Interstate Commerce Commission in 1887. The ICC brought uniformity to railroad regulation and curbed the discriminatory practices of the state commissions.⁴³ That the railroads are a kind of public utility, state-regulated monopolies, is the starting point of the inquiry into the nature of their obligation to serve the public.

The railroad's obligation to serve the public can be measured by its freedom to respond to market conditions in the conduct of its business, to act as a profit-maximizing firm, and to withdraw from unprofitable ventures. In the context of railroad bankruptcy and reorganization, the pertinent question is to what extent may a railroad terminate service or abandon a line when the service or line has become unprofitable?

39. For an interesting history of government sponsorship of the first American railroads, see, R. SOBEL, *supra* note 27, at 1-47 (1977).

40. See, e.g., An Act to aid in the Construction of a Railroad and Telegraph Line from the Missouri River to the Pacific Ocean, and to secure to the Government the Use of the same for Postal, Military, and Other Purposes, ch. 120, § 3, 12 Stat. 489 (1862).

41. See generally C. CHERINGTON, THE REGULATION OF RAILROAD ABANDONMENTS (1948); M. CONANT, RAILROAD MERGERS AND ABANDONMENTS (1964). See, e.g., *Gates v. The Boston & N.Y. Air Line R.R.*, 53 Conn. 333, 5 A. 695 (1885); *Southern Ry. v. Franklin & P.R.R.*, 96 Va. 693, 32 S.E. 485 (1899).

42. See, e.g., *State ex rel Naylor v. Dodge City, M. & T.R.R.*, 53 Kan. 377, 36 P. 747 (1894); *Hinckley v. Kettle River R.R.*, 70 Minn. 105, 72 N.W. 835 (1897).

43. "The principal objects of the Interstate Commerce Act were to secure just and reasonable charges for transportation; to prohibit unjust discriminations in the rendition of like services under similar circumstances and conditions; to prevent undue or unreasonable preferences to persons, corporations or localities; to inhibit greater compensation for a shorter than for a longer distance over the same line; and to abolish combinations for the pooling of freights." *ICC v. Baltimore & O. R.R.*, 145 U.S. 263, 276 (1892). See generally G. KOLKO, RAILROADS AND REGULATION: 1877-1916 (1965); I. SCHARFMAN, THE INTERSTATE COMMERCE COMMISSION (1931). The Interstate Commerce Act was recently revised, codified, and enacted into title 49 of the United States Code. Revised Interstate Commerce Act, Pub. L. 95-473, § 1, 82 Stat. 1337 (Oct. 17, 1978). The Act "may not be construed as making substantive changes in the laws replaced." *Id.* at § 3.

With respect to both service termination and line abandonment, Congress has enacted specific statutes⁴⁴ that impose a balancing test under which the public's need for convenient rail service is weighed against the burden of such service on interstate commerce. Thus, in the case of service terminations, the ICC may order the restoration of service sought to be abandoned if the service is "required or permitted by present or future public convenience and necessity and will not unreasonably burden interstate or foreign commerce. . . ."⁴⁵

There are few determinative rules in applying this test. Upon the 1958 enactment of the service termination statute as section 13a of the Interstate Commerce Act, the Senate reported that its purpose was to authorize the termination of rail services that "no longer pay their way and for which there is no longer sufficient public need to justify the heavy financial losses entailed."⁴⁶ In *Southern Railway v. North Carolina*,⁴⁷ a case involving a petition by the interstate carrier to terminate two intrastate passenger trains, the Supreme Court reviewed the legislative history of the statute and established two general rules for the application of the balancing test. First, the profitability of the train service, or lack thereof, may be considered as an element in the balance, but the fact that the train service is presently unprofitable does not, by itself, authorize its termination.⁴⁸ Consequently, a railroad may be required to operate an unprofitable train. Secondly, the overall profitability of the railroad may be considered as a factor in the decision to permit termination of service, but the fact that the railroad as a whole is profitable does not require a decision to continue the service.⁴⁹ The Court did not decide the converse of the issues presented by these two rules: (1) whether abandonment is permissible when the service itself is profitable; and (2) whether abandonment is impermissible even when the railroad, as a system, is unprofitable. Presumably, no instances of the former case will arise; and, in the latter case, unless the railroad is suffering only temporary business decline, it will probably seek the protection of bankruptcy reorganization. The unprofitability of the service to be terminated and the overall profitability of the railroad are relevant factors only to the extent that they reveal the ability

44. 49 U.S.C.A. § 10903 (West 1979) (abandonment of lines) (replacing 49 U.S.C. § 1a (1976)); 49 U.S.C.A. § 10908 (West 1979) (discontinuance of service) (replacing 49 U.S.C. § 13a (1976)). A "service termination" involves the discontinuance of a particular kind of service, *e.g.*, passenger operation, along a particular line while retaining other service, *e.g.*, freight operation, along the same line. A "line abandonment" entails termination of all service along a line and usually involves physical removal of the trackage.

45. 49 U.S.C.A. § 10908(c) (West 1979).

46. S. REP. NO. 1647, 85th Cong., 2d Sess. 21 (1958).

47. 376 U.S. 93 (1964).

48. *Id.* at 104.

49. *Id.* at 104-05.

of the railroad to absorb the local loss without harm to its interstate service.

By contrast, line abandonment operates under what might be called the Certificate System. The Interstate Commerce Act was amended in 1920 to prohibit a railroad from engaging in any new rail construction or line extension without a certificate from the ICC stating that "the present or future public convenience and necessity require or will be enhanced by . . . such extended or additional line of railroad."⁵⁰ Abandonment requires a similar certificate; "the present or future public convenience and necessity require or permit the abandonment or discontinuance."⁵¹

This Certificate System is an outgrowth of the relationship which the early railroads enjoyed with the state of their charter, the state franchise or charter was construed as a contract between the carrier and the public.⁵² The Supreme Court, in *Chesapeake & Ohio Railway v. Public Service Commission*,⁵³ stated:

One of the duties of a railroad company doing business as a common carrier is that of providing reasonably adequate facilities for serving the public. This duty arises out of the acceptance and enjoyment of the powers and privileges granted by the State and endures so long as they are retained. It represents a part of what the company undertakes to do in return for them, and its performance cannot be avoided merely because it will be attended by some pecuniary loss.⁵⁴

In *Fort Smith Light & Traction Company v. Bourland*,⁵⁵ the Court held that a local loss did not warrant termination of the local line. Rather, the Court required the traction company to choose between abandoning its entire operation and returning its franchise to the city or, alternatively, operating the entire franchise at a loss, even though the loss was attributable to the one local line.

The requirement that a railroad obtain an ICC certificate of "public convenience and necessity" before engaging in any new construction serves two functions. First, it is a means by which the ICC can prevent over construction by financially weak carriers and the inefficient duplication of routes. Rationalization of the nation's rail system is particu-

50. 49 U.S.C. § 1(18)(a) (1976) (originally enacted Feb. 28, 1920, ch. 91, § 402, 41 Stat. 477). The Revised Interstate Commerce Act requires that the ICC find that "public convenience and necessity require or will be enhanced by the construction or acquisition (or both) and operation of the railroad line." 49 U.S.C.A. § 10901(a) (West 1979).

51. 49 U.S.C.A. § 10903(a) (West 1979) (replacing 49 U.S.C. § 1a(1) (1976)). The current version adds that "the Commission shall consider whether the abandonment or discontinuance will have a serious, adverse impact on rural and community development." *Id.*

52. See generally C. CHERINGTON, *supra* note 41.

53. 242 U.S. 603 (1917).

54. *Id.* at 607.

55. 267 U.S. 330 (1925).

larly important in light of the fact that total route miles of trackage has been declining throughout this century as other forms of transportation have developed.⁵⁶ Secondly, the Certificate System provides the legal framework (the contract between the carrier and the public) under which the carrier's freedom to abandon a line may be regulated. The certificate of public convenience and necessity embodies the obligation of the carrier to render continuous service to the public.⁵⁷

Early judicial interpretation of the "public convenience and necessity" test indicated that the phrase itself involves a balancing of carrier and shipper interests. In *Colorado v. United States*,⁵⁸ the state of Colorado sought to protect local industry by challenging the ICC's approval of a carrier's request to abandon intrastate line. In upholding the ICC's decision, Justice Brandeis held that the "public convenience and necessity" standard requires consideration of the burden on interstate commerce imposed by the unprofitable line.⁵⁹ Thus, the determination of public need for a particular line involves a balancing of the local dependency upon continued rail service and the burden of the unprofitable service upon the shipping public at large.

In actual practice, the ICC has eschewed consideration of carrier prosperity and has balanced the losses suffered by the specific carrier against the losses to be suffered by the local public in the event of abandonment.⁶⁰ In this regard, the volume of local traffic and the dependency of local industry on rail transportation are the most critical factors. The difficult cases involve rail-dependent industries such as coal mines or grain elevators. A study of such cases has observed that "[t]he result always depends upon balancing the sum total of such individual losses against the operating deficit being incurred by the appli-

56. In 1930, the nation had 230,602 miles of track in freight service. By 1960, there were only 208,043 miles. See INTERSTATE COMMERCE COMMISSION, STATISTICS OF RAILWAYS IN THE UNITED STATES (1920-1953) (published yearly); INTERSTATE COMMERCE COMMISSION, TRANSPORT STATISTICS IN THE UNITED STATES (1954-1978) (published yearly).

57. See *Colorado v. United States*, 271 U.S. 153 (1926). "The charter of the Colorado & Southern," declared Justice Brandeis, "is a contract with the State. By accepting the charter, the Company assumed the obligation of providing intrastate service on every part of its line within the State. . . ." *Id.* at 161-62.

58. 271 U.S. 153 (1926).

59. *Id.* at 169.

60. See generally C. CHERINGTON, *supra* note 41, at 125-36. This approach is not without judicial approval. "In many cases, it is clear that the extent of the whole traffic, the degree of dependence of the communities directly affected upon the particular means of transportation, and other attendant conditions, are such that the carrier may not justly be required to continue to bear the financial loss necessarily entailed by operation. In some cases, although the volume of the whole traffic is small, the question is whether abandonment may justly be permitted, in view of the fact that it would subject the communities directly affected to serious injury while continued operation would impose a relatively light burden upon a prosperous carrier." *Colorado v. United States*, 271 U.S. 153, 168-69 (1925).

cant.”⁶¹ Since individual circumstances predominate in the ICC decision, there are but a few general rules: the line must be unprofitable before abandonment will be permitted; there must be rail-dependent industries before abandonment will be prevented; and, overall prosperity of the carrier is only tangentially relevant, if at all.

Notwithstanding the restrictions placed on line abandonment by the Certificate System or by a carrier's charter, there is a point at which continued operation by an unprofitable carrier cannot be compelled. In *Brooks-Scanlon Co. v. Railroad Commission*, the Supreme Court held that where there is no reasonable hope of future profitable operation, the privately financed railroad cannot be compelled to continue its service to the public.⁶² The case involved an unprofitable feeder line abandoned by its profitable lumber-company owner. The Railroad Commission for the state of Louisiana issued an order to show cause as to why service on the line should not be reinstated. Despite a showing that the line was unprofitable, the Commission concluded that service could be compelled provided the overall enterprise—carriage and mill—was profitable.⁶³ The Supreme Court reversed and, in an opinion by Justice Holmes, held:

It is true that if a railroad continues to exercise the power conferred upon it by a charter from a State, the State may require it to fulfil an obligation imposed by the charter even though fulfilment in that particular may cause a loss. . . . But that special rule is far from throwing any doubt upon a general principle too well established to need further argument here. . . . If the plaintiff be taken to have granted to the public an interest in the use of the railroad it may withdraw its grant by discontinuing the use when that use can be kept up only at a loss.⁶⁴

This holding was quickly affirmed by two subsequent cases: *Bullock v. Florida ex rel. Railroad Commission*⁶⁵ and *Railroad Commission v. Eastern Texas Railroad*.⁶⁶ In each case the Supreme Court permitted the railroad to replace service with salvage on the theory that compelled operation at a loss would be an unconstitutional taking of property for public use. In the latter case the Court stated: “The controlling principle is the same that is applied in the many cases in which the constitutionality of a rate is held to depend upon whether it yields a fair return.”⁶⁷

In their subsequent application, however, these holdings have

61. C. CHERINGTON, *supra* note 41, at 133.

62. 251 U.S. 396, 399 (1926).

63. *Id.* at 398.

64. *Id.* at 399.

65. 254 U.S. 513 (1921).

66. 264 U.S. 79 (1924).

67. *Id.* at 85. *See also* 251 U.S. at 399.

been limited. *Brooks-Scanlon* was decided almost one month before the enactment of legislation giving the ICC jurisdiction over route extension and abandonment.⁶⁸ *Bullock*, decided a year later, portended the eventual application of the Certificate System. In that case, the Court qualified the *Brooks-Scanlon* holding: "Without previous statute or contract to compel the company to keep on at a loss would be an unconstitutional taking of its property."⁶⁹ Similarly, in *Eastern Texas*, the Court distinguished between permissive and impermissive charters: only the permissive charter creates no obligation to serve the public at a loss.⁷⁰ An ICC certificate that an abandonment is permitted without harm to the public's convenience and necessity is a statutory condition of abandonment; it is not a "permissive" charter. Thus in the context of abandonment by carriers within ICC jurisdiction, the formality of obtaining a certificate of abandonment becomes a condition precedent to legal cessation of service. In *Meyers v. Jay Street Connecting Railroad*,⁷¹ the carrier petitioned the ICC for a certificate permitting abandonment of all service, but, prior to any regulatory approval, announced cessation of operation. Despite the railroad's unprofitability, an injunction forbidding termination of service was sustained pending issuance or denial of an abandonment certificate.⁷² If the *Brooks-Scanlon* doctrine has any remaining life, it is applied only in instances where the ICC lacks jurisdiction or as a parameter within which the ICC must consider abandonment petitions.⁷³

Although railroads earn a notoriously low return on their investment,⁷⁴ it is rare that a railroad, even in bankruptcy reorganization, has

68. *Brooks-Scanlon* was decided February 2, 1920; the Interstate Commerce Act was amended February 28, 1920. See note 50 *supra*.

69. 254 U.S. at 521 (emphasis added).

70. 264 U.S. at 85. A charter is "permissive" if, under its terms, the grantee company is authorized but not required to engage in rail operation. Such charters are more akin to licenses such as those typically granted to taxi companies. Withdrawal from operation is permitted by economic necessity. The impermissive charter binds the grantee company, upon its acceptance, to perpetual service along the route of the charter.

71. 259 F.2d 532 (2d Cir. 1958).

72. *Id.* at 535.

73. To the extent that the ICC retains jurisdiction over line and service abandonments during the reorganization process, the bankrupt railroad may not terminate service absent the appropriate ICC certificate. Prior to the Reform Act, the ICC did have such jurisdiction. 11 U.S.C. § 205 (1976) (amended 1978); *In re Central R.R. of N.J.*, 485 F.2d 208 (3d Cir. 1973), *cert. denied*, 414 U.S. 1131 (1974). Under the Reform Act, the ICC may express its opinion regarding proposed abandonments, but the bankruptcy court is empowered to grant abandonment over the objection of the Commission. Reform Act, *supra* note 3, § 1170.

74. See generally MOODY'S TRANSPORTATION MANUAL (1978) [hereinafter cited as MOODY'S]. In the 1966-78 period, the return on investment, after adjustment for depreciation, fell from a high 3.9% in 1966 to a low of 0.83% in 1978. Even more striking, net income in constant 1966 dollars fell from \$904 million to \$27 million. *As earnings sagged, improvement outlays rose*, RAILWAY AGE, Jan. 30, 1978, at 59; *Record-high activity, but little profit*,

no hope of regaining profitability. Hence, the first condition of the *Brooks-Scanlon* doctrine—that there be no reasonable expectation of future profits—is rarely met. The exceptional case was the bankruptcy of the New York, New Haven & Hartford Railroad in 1961. Without hope of profitable operation, its liquidation was threatened by the district court in 1968 under the *Brooks-Scanlon* holding.⁷⁵ Only its forced participation in the merger of the New York Central and Pennsylvania Railroads avoided wholesale termination of service.⁷⁶ Recent history has not, however, afforded any other tests of the continued viability of *Brooks-Scanlon*.⁷⁷

In summary, the rail carrier's obligation to serve the public is created by the carrier's acceptance of its franchise and by the Certificate System, under which new lines are constructed and old lines abandoned only if required or permitted by public convenience and necessity. The obligation may be avoided only if the railroad is hopelessly unprofitable and, even then, only if it is outside the jurisdiction of the ICC or made subject to an order in excess of the ICC's authority.

The next section explores the public interest in continued rail service, historically the fundamental concern of the ICC. The section first examines the recent experiments in nationally funded rail service—Amtrak and Conrail—and then discusses the impact of continued service on the rights of creditors of insolvent carriers.

III. The Public Interest in Being Served

A. Government Funding of Rail Service

From almost the first iron spike, but certainly to Amtrak's latest concrete tie,⁷⁸ the federal government's interest in railroads has been nothing short of intense. Railroads were the vehicle by which the nation expanded; they were the catalyst necessary for economic development. The transcontinentals received land grants as a means of financing construction.⁷⁹ The Interstate Commerce Commission was

RAILWAY AGE, Jan. 29, 1979, at 60. With that kind of performance, the railroads would do better by liquidating their assets and purchasing government securities.

75. *In re New York, N.H. & H.R.R.*, 289 F. Supp. 451, 459 (D. Conn. 1968).

76. Some passenger service was abandoned with ICC permission under 49 U.S.C. § 13a (1976) (current version at 49 U.S.C.A. § 10908 (West 1979)) as being an undue burden on interstate commerce and permitted by public convenience and necessity. *E.g.*, *New York, N.H. & H.R.R., Trustees, Discontinuance of Passenger Service between Boston and Needham Heights, West Medway, Blackstone and Dedham, Mass.*, 327 I.C.C. 77 (1965).

77. *See In re Penn Central Transp. Co.*, 494 F.2d 270, 278-82 (3d Cir. 1974), *cert. denied*, 419 U.S. 883 (1974); *In re Penn Central Transp. Co.*, 347 F. Supp. 1356, 1366 (E.D. Pa. 1972).

78. *Why DOT opted for concrete ties in the Northeast Corridor*, RAILWAY AGE, Sept. 12, 1977, at 32-34.

79. *See note 40 supra.*

created to nationalize rate regulation;⁸⁰ its jurisdiction subsequently expanded to include new construction, abandonment, consolidations and mergers, as well as regulation of the trucking industry.⁸¹ Rail labor has its very own act,⁸² as does retired rail labor.⁸³ Safety,⁸⁴ employer liability,⁸⁵ hours of employment,⁸⁶ boiler inspection,⁸⁷ unemployment insurance⁸⁸ and ashpans⁸⁹ have all been the subjects of separate and distinct Congressional Acts. With all this government regulation of and interest in the nation's railroads, and their characteristic low return on investment and many bankruptcies, why is it that the industry has not been nationalized? One answer is that the obligation of the common carrier to serve the public, described in the previous section as unconditional save in the rare instance of hopeless insolvency, precludes any need for public funding of deficit operations except when the private sector cannot be compelled to provide further capital. In this writer's view of history, the exhaustion of private capital is precisely what forced Congress to enact the Amtrak⁹⁰ and Conrail⁹¹ legislation. Each

80. See note 43 *supra*.

81. "It is hereby declared to be the national transportation policy of the Congress to provide for fair and impartial regulation of all modes of transportation subject to the provisions of this Act, so administered as to recognize and preserve the inherent advantages of each; to promote safe, adequate, economical, and efficient service and foster sound economic conditions in transportation and among the several carriers; to encourage the establishment and maintenance of reasonable charges for transportation services, without unjust discriminations, undue preferences or advantages, or unfair or destructive competitive practices; to cooperate with the several States and the duly authorized officials thereof; and to encourage fair wages and equitable working conditions;—all to the end of developing, coordinating, and preserving a national transportation system by water, highway, and rail, as well as other means, adequate to meet the needs of the commerce of the United States, of the Postal Service, and of the national defense." Act of Sept. 18, 1940, ch. 722, § 1, 54 Stat. 899. See 49 U.S.C. § 1(18) (1976) (added by Act of Feb. 28, 1920, ch. 91, § 402, 41 Stat. 477) (current version at 49 U.S.C.A. § 10901 (West 1979)) (new construction); 49 U.S.C. § 5(2) (1976) (added by Act of Feb. 28, 1920, ch. 91, § 407, 41 Stat. 480) (current version at 49 U.S.C.A. §§ 11342-47 (West 1979)) (mergers and consolidations); 49 U.S.C. § 1a (1976) (first enacted as 49 U.S.C. § 1(19)-(20) by Act of Feb. 28, 1920, ch. 91, § 402, 41 Stat. 478) (amended and renumbered Act of Feb. 5, 1976, Pub. L. No. 94-210, § 802, 90 Stat. 127) (current version at 49 U.S.C.A. § 10903 (West 1979)) (abandonments).

82. Railway Labor Act, ch. 347, § 1, 44 Stat. 577 (1926) (amended seven times).

83. Railroad Retirement Act of 1937, ch. 382, 50 Stat. 307 (amended 42 times); Railroad Retirement Act of 1974, Pub. L. No. 93-445, 88 Stat. 1305-1361 (amended 3 times). See also Railroad Retirement Tax Act, ch. 709, 60 Stat. 722 (1946) (amended eleven times).

84. Act of Oct. 16, 1970, Pub. L. No. 91-458, 84 Stat. 971.

85. Employer's Liability Act, ch. 3073, 34 Stat. 232 (1906) (first of four such acts).

86. Hours of Service Act, ch. 2939, 34 Stat. 1415 (1907) (first of four such acts).

87. Boiler Inspection Act, ch. 103, 36 Stat. 913 (1911) (first of seven such acts).

88. Railroad Unemployment Insurance Act, ch. 680, 52 Stat. 1094 (1938) (amended 23 times).

89. Ash Pan Act, ch. 225, 35 Stat. 476 (1908) (never amended).

90. Rail Passenger Service Act of 1970, Pub. L. No. 91-518, 84 Stat. 1327 (codified in 45 U.S.C. §§ 501-645 (1976)).

is an instance in which continued rail service in the public interest could only be preserved by public financing.

Amtrak is the result of system-wide unprofitability and deterioration of the nation's passenger trains in the 1950-1970 era. During this period, otherwise profitable railroads were burdened by unprofitable service. Rather than force railroad freight operations to forever subsidize passenger service, Congress created a semi-public corporation—The National Railroad Passenger Corporation—to assume the responsibility of providing passenger rail service.⁹² In exchange for cash and/or passenger equipment, according to a formula based on a percentage of the carrier's passenger deficits, the railroads received common stock in the corporation and each was relieved of "its responsibilities as a common carrier of passengers by rail in intercity rail passenger service. . . ."⁹³ The corporation commonly known as Amtrak, assumed this responsibility and was entitled to contract with the participating railroads for the use of their tracks and facilities.⁹⁴ But the creation of a national passenger railroad has not closed the gap between operating costs and fare revenues. Since 1970, Congress has appropriated more than three billion dollars for the corporation's net operating expenses.⁹⁵ Additionally, loan guarantees of \$900 million and direct grants of \$463 million have been extended for capital projects.⁹⁶

Unlike the problem that led to the creation of Amtrak, which involved essentially profitable railroads burdened with an unprofitable service, the crisis that preceded the creation of the Consolidated Rail Corporation involved the financial collapse of all major carriers in the northeast.⁹⁷ The first to enter bankruptcy was the Central Railroad of New Jersey in 1967.⁹⁸ Three years later, the largest carrier, the Penn Central Transportation Company, filed its petition.⁹⁹ The four remaining railways quickly followed.¹⁰⁰ Almost three years after the filing of

91. Regional Rail Reorganization Act of 1974, Pub. L. No. 93-236, 87 Stat. 985 (codified in 45 U.S.C. §§ 701-94 (1976)).

92. 45 U.S.C. § 541 (1976). Of the seventeen directors of the National Railroad Passenger Corporation, one is the Secretary of Transportation, another is the President of the corporation, eight are appointed with Senate approval by the President of the United States; three are elected by common stockholders and four are elected by preferred stockholders. *Id.* § 543.

93. 45 U.S.C. § 561 (1976).

94. *Id.*

95. MOODY'S, *supra* note 74, at 708.

96. *Id.*

97. *See generally* R. SOBEL, *supra* note 27.

98. MOODY'S, *supra* note 74, at 416.

99. *Id.* at 332. The filing date was June 21, 1970.

100. The Lehigh Valley Railroad Company filed on July 24, 1970. *Id.* The Philadelphia & Reading Railroad Company filed on November 23, 1971. *Id.* at 407. They were followed

Penn Central's petition in bankruptcy, the district court expressed serious doubt that the railroad could be reorganized without government assistance.¹⁰¹ The court threatened to order cessation of all operations as of October 1, 1973, with liquidation to follow as soon as practical, unless a definitive reorganization plan was presented to the court by July 2, 1973.¹⁰² Congress responded quickly with the Regional Rail Reorganization Act of 1973,¹⁰³ creating two entities: the United States Railway Association (USRA),¹⁰⁴ a non-profit association whose duties include the design of a final system plan for the Northeast,¹⁰⁵ and the Consolidated Rail Corporation (Conrail),¹⁰⁶ whose principal function is the operation of the rationalized system.¹⁰⁷ Conrail's Series B preferred and common stock were exchanged for the rail properties of the six bankrupt railroads, and Series A preferred stock and debentures were issued to the USRA.¹⁰⁸ USRA functions as a conduit for government aid, which as of the first quarter of 1979 totaled \$2.154 billion dollars.¹⁰⁹ Despite the words of the enabling act that "[t]he final system plan shall be formulated in such a way as to effectuate . . . the creation, through a process of reorganization, of a financially self-sustaining rail and express service system,"¹¹⁰ a viable railroad is yet to be created.¹¹¹

Why did the unprofitability of the American passenger train and the collapse of the major northeast railroads deserve government bailouts, when ordinary and singular bankruptcy reorganizations did not? It was not a more intense public interest in continued rail service

by the Erie Lackawanna Railroad Company on June 26, 1972, *Id.* at 320, and the Lehigh and Hudson Rivers Railway Company.

101. *In re Penn Central Transp. Co.*, 355 F. Supp. 1343, 1345 (E.D. Pa. 1973).

102. *Id.* at 1346. A plan was filed by July 2, 1978, and the court ordered immediate filing with the ICC and requested certification by the latter by October 31, 1978. *In re Penn Central Transp. Co.*, 363 F. Supp. 1263, 1267 (E.D. Pa. 1973).

103. *Supra* note 91.

104. 45 U.S.C. § 711 (1976).

105. *Id.* § 712(a)(1).

106. *Id.* § 741(a).

107. *Id.* § 742.

108. *Id.* § 741(e).

109. RAILWAY AGE, Jan. 29, 1979, at 4.

110. 45 U.S.C. § 716(a)(1) (1976).

111. On December 1, 1978, Conrail Chairman Edward J. Jordan stated: "At this time, Conrail is losing 10 cents for every dollar of freight revenue it receives. Obviously, Conrail has too much unprofitable traffic on too much plant. But plant reduction decisions made on the present rate-making and abandonment process do not address the root causes of non-compensatory traffic." *Conrail Defers Line Abandonments*, RAILWAY AGE, Dec. 25, 1978, at 12. *But see* RAILWAY AGE, July 30, 1979, at 14, which reports that Conrail enjoyed a second quarter, 1979, profit of \$29.4 million. Conrail Chairman Jordan is reported as saying: "The Northeast section of the nation now has a reliable freight transportation system in Conrail. Conrail is ready to serve its customers to a better degree than ever in its brief history and in the recent history of its predecessors."

that warranted national aid to the bankrupt Penn Central¹¹² but not to a predecessor bankrupt, the New Haven.¹¹³ Rather, the semi-public Amtrak and Conrail were born of necessity, with no private source of capital available and no other means to prevent termination of service. Unprofitable rail passenger service by the private carriers could not be compelled indefinitely under the termination of service statute.¹¹⁴ At some point the burden on the carriers' ability to provide efficient interstate freight service would outweigh any further need for passenger trains. Some kind of nationalization was the only means of preserving a national rail passenger system. Similarly, the Conrail legislation was compelled by the threat of liquidation of the Penn Central.¹¹⁵ Private capital was no longer available to fund a continued deficit operation. However, a different situation prevailed when the New Haven collapsed. In that instance, quite conveniently, the Pennsylvania and New York Central Railroads were discussing merger and could be, and were, compelled to include the New Haven, operate trains and absorb its losses.¹¹⁶

The Amtrak and Conrail experiments in nationalization illustrate the extreme to which a creditor may be required to dedicate his security interest to public service. After the *New Haven Inclusion Cases*, there appears to be no ascertainable outer limit at which public funds are required, constitutionally, to pick up the tab for continued rail operation.¹¹⁷ Pragmatic necessity, not some rule of law, opens the federal pocketbook in the aid of dying carriers.

B. The Public Interest and Creditor Rights

What justifies continued deficit operation of a railroad during reorganization and subsequent approval of a reorganization plan which adversely and materially affects the value of the creditors' claims? It is frequently asserted that during reorganization, the normal rights of the creditor may be suspended for a reasonable period. This assertion, however, does not explain why impairment of a creditor's estate during such a period is not a taking of private property for public use.¹¹⁸ The Fifth Amendment prohibition of uncompensated public takings functions as a constitutional parameter to any act of the federal govern-

112. See notes 97-110 *supra*.

113. See notes 25-33 and accompanying text *supra*.

114. 49 U.S.C. § 13a (1976) (current version at 11 U.S.C.A. § 10903 (West 1979)). See text and notes in Section II *supra*.

115. See notes 101-02 *supra*.

116. *New Haven Inclusion Cases*, 399 U.S. 392 (1970). See 49 U.S.C. § 5(2) (1976) (current version at 11 U.S.C.A. §§ 11343-11347 (West 1979)).

117. See text accompanying notes 25-36 *supra*.

118. See note 24 *supra*.

ment, including the operation of the bankruptcy laws.¹¹⁹ Hence, any suspension of the rights of the creditor during the reorganization process cannot permanently enjoin the right to compensation when the creditor's property is taken for a public purpose. Therefore, simply stating, as two courts have done,¹²⁰ that during reorganization the creditor's rights may be suspended for a reasonable period of time does not rebut the creditor's Fifth Amendment argument; some further assertion is required. Two such arguments have been advanced: first, that there is indeed a taking of the creditor's property, but that he has, in some manner, waived his right to Fifth Amendment protection; and second, that there is no taking of property at all.

Support for the view that the creditor has waived his Fifth Amendment right to compensation for any public taking of his property can be found in *Reconstruction Finance Corporation*. In some addendum remarks, the Court asserted that the investor in a railroad "assumes the risk" that his property will be dedicated to public service.¹²¹ The idea is that even though the bankruptcy and reorganization of a railroad may necessitate some deterioration or impairment of the creditor's security in order to prevent any termination of publicly needed service, no creditor is ever compelled by the government to place his funds at such risk. Given voluntary investment and foreknowledge of the bankruptcy laws, the investor can hardly complain when a foreseen but low probability down-side risk is realized. The public's interest in continued rail service does not itself justify suspension of the creditor's rights and the deterioration of his estate, but satisfaction of the public's desire for continued rail service at the expense of the creditor is permissible where in accord with the government's past practice, and the creditor's notice and acceptance of the risk.

Provided there is some past practice that one wishes to perpetuate, the argument provides a justifying rationale. It does not, however, justify the past practice itself. Yet, uncompensated takings of private property for public use are constitutionally prohibited.¹²² But if illegal, how can the operation of the bankruptcy laws, themselves subject to the Fifth Amendment, give rise to a past practice of uncompensated takings—the risk which the creditor ostensibly assumes. The waiver theory is an incomplete, if not unsatisfactory, justification for court ordered rail service at private expense.

The alternative argument is that there is no public taking of the creditor's security interest even though the assets of the railroad are eroding during the reorganization. This proposition would be most

119. *Louisville Joint Stock Land Bank v. Radford*, 295 U.S. 555, 589 (1935).

120. *See* note 24 *supra*.

121. 328 U.S. at 535-36.

122. U.S. CONST. amend. V.

plausible if, upon approval or a reorganization plan, the creditors received property equal to the liquidation value of their claims as of the date of the initial bankruptcy. Forced operation of the railroad during the reorganization, in lieu of liquidation, would not cause the creditor to be in any worse position than if liquidation had occurred immediately.

Some commentators¹²³ have asserted that this argument represents the essential teaching of *Continental Illinois National Bank & Trust Company v. Chicago, Rock Island & Pacific Railway*.¹²⁴ In that case, the bankruptcy court enjoined the secured creditors from forcing a foreclosure sale of the carrier's pledged property, whose value far exceeded the carrier's obligations. The Supreme Court upheld the injunction on the ground that legislation drawn under the constitutional authority of Congress to enact uniform bankruptcy laws may incidentally impair private contract.¹²⁵ In *Continental Illinois*, the injunction went "no further than to delay the enforcement" of debenture agreements.¹²⁶ Referring to the possible decline in value of the pledged security during the duration of the injunction, the Court stated that "[a] claim that injurious consequences will result to the pledgee . . . may not, of course, be disregarded. . . ."¹²⁷ Since in this case the value of the pledged security far exceeded the value of creditor's claims,¹²⁸ the mere delay in satisfaction caused no irremediable harm.

Surprisingly, the Supreme Court in the *New Haven Inclusion Cases* cited *Continental Illinois* in support of its holding that creditor rights are not absolute.¹²⁹ In the *Inclusion Cases*, the Court held that a mortgage bond holder may be delayed in attempts to reach the security even if the delay causes irremediable loss. Whether a suspension of remedial rights is injurious to the creditor "presents a question addressed not to the power of the court but to its discretion—a matter not subject to the interference of an appellate court unless such discretion be improvidently exercised."¹³⁰ The Court *certainly* did not understand *Continental Illinois* to prohibit the suspension of creditor rights when there is great likelihood of harm.

The Court's substantive holding—that there was no uncompen-

123. See Note, *Assuring Adequate Rail Service: The Conflict Between Private Rights and Public Needs*, 45 *FORDHAM L. REV.* 1429, 1434-35 (1977); Note, *Takings and the Public Interest in Railroad Reorganization*, 82 *YALE L.J.* 1004, 1011-14 (1973).

124. 294 U.S. 648 (1935).

125. *Id.* at 680.

126. *Id.* at 681.

127. *Id.* at 677.

128. See *id.* at 658-59.

129. 399 U.S. at 420.

130. *Id.* at 490-91 (quoting *Continental Illinois Nat'l Bank & Trust Co. v. Chicago, R.I. & P. Ry.*, 294 U.S. 648, 677 (1934)).

sated taking of the property of the New Haven creditors—rests upon Justice Reed's opinion in *Reconstruction Finance Corporation* that the creditor invests funds in a public utility with an obligation to serve the public, and therefore in reorganization the interests of both creditor and public are considered.¹³¹ Justice Brandeis has described the carrier's obligation as a "contract with the State."¹³² The essence of his argument is that the creditor, by investing in a railroad, subordinates his rights to the obligation of the carrier to serve the public and may not reclaim his funds in a manner that would jeopardize the carrier's ability to satisfy its obligation. The creditor has not waived his Fifth Amendment right to compensation for any public taking of his estate. Rather, he has so aligned himself with the carrier that during bankruptcy reorganization, when the railroad's continued ability to serve the public is most in doubt, there is no taking of the creditor's estate absent the unlawful demand that the railroad itself continue operation. The creditor's loss is instead characterized as the realization of a foreseeable risk. As noted in Section I, the carrier's obligation to serve the public admits of few exceptions, and it is not surprising that the railroad's creditor, having assumed the obligation of the carrier with his investment, may not freely withdraw his funds when the carrier enters bankruptcy reorganization.

The next section reviews the provisions of the Bankruptcy Reform Act of 1978 as they pertain to railroad reorganization and the taking problem developed in this note. Various versions of the bill will be discussed.

IV. Reorganization Reform

Prior to the Bankruptcy Reform Act of 1978,¹³³ a plan of reorganization was required to be drafted and submitted by the debtor-railroad to both the bankruptcy court and the Interstate Commerce Commission.¹³⁴ Such a plan would "include provisions modifying or altering the rights of creditors . . . through the issuance of new securities. . . ."¹³⁵ After public hearings, the Commission would certify a plan, though not necessarily the one submitted, which "in its opinion . . . will be compatible with the public interest. . . ."¹³⁶ Once a plan had been certified by the Commission, the court would request that all affected parties state their objections to the plan as well as any claims

131. 328 U.S. at 535-36.

132. *Colorado v. United States*, 271 U.S. 153, 161-62 (1926).

133. *See* note 3 *supra*.

134. 11 U.S.C. § 205(d) (1976) (amended 1978).

135. *Id.* § 205(b).

136. *Id.* § 205(d).

for equitable treatment.¹³⁷ Thereafter, the court either would approve the plan if, *inter alia*, it was fair and equitable,¹³⁸ or would disapprove the plan and either dismiss the proceedings or refer the plan back to the Commission.¹³⁹ Once the interchange between the court and the ICC had resulted in an approved plan, each class of creditors would be requested to express either its acceptance or rejection.¹⁴⁰ If two-thirds of the actual vote of each class (as measured by the dollar volume of its claims) approved the plan, then it would be confirmed by the court.¹⁴¹ Should any class of creditors or stockholders reject the plan, the court could nevertheless confirm the plan upon a finding that such rejection was not "reasonably justified in the light of . . . all the relevant facts."¹⁴²

The central feature of this process of certification, approbation and confirmation is the joint jurisdiction of the Interstate Commerce Commission and the bankruptcy court. The Commission functions as the voice of the public and the advocate of the public's interest, while the bankruptcy court functions as an adjudicatory body, balancing the interests of the creditors once the Commission certifies that the plan conforms to the public interest.

The natural consequence of this joint responsibility is the considerable and exasperating delay between the filing of the initial petition in bankruptcy and the final confirmation of a reorganization plan. The lapse of time is often considerable, the longest being twenty-three years for the final reorganization of the Missouri Pacific Railway.¹⁴³ During this period, the creditor's right to his security is suspended. No interest need be paid on any debt, and often the value of the railroad's assets deteriorates. It is not uncommon for the asset value of the reorganized railroad to be less than the liquidation value of the railroad upon initial bankruptcy.¹⁴⁴ Nor is it surprising that the railroad's creditors have objected loudly to such a tedious reorganization process, a process that often leaves them with less satisfaction of their claims than if the rail-

137. *Id.* § 205(e).

138. *Id.*

139. *Id.*

140. *Id.*

141. *Id.*

142. *Id.*

143. The Missouri Pacific Railroad was in reorganization from 1933 to 1956. MOODY'S, *supra* note 74, at 248. Long reorganizations do not always result in a financially sound company. The Chicago, Rock Island & Pacific Railroad, which entered bankruptcy reorganization on March 17, 1975, had previously been reorganized during the fourteen-year period between 1933 and 1947. *Id.* at 133.

144. This was precisely the plight of the creditors of the New York, New Haven and Hartford Railroad and the source of complaint in the New Haven Inclusion Cases, 399 U.S. 392 (1970).

road had been sold for scrap.¹⁴⁵

Reform of the bankruptcy law has proceeded concurrently in both the House of Representatives and the Senate. The Commission on the Bankruptcy Laws of the United States was created by Congress in 1970 to review and recommend changes to the Bankruptcy Act.¹⁴⁶ In 1973, the Commission reported its findings and proposed a draft bill, which was submitted to the 93rd Congress as H.R. 10792¹⁴⁷ and S. 4026.¹⁴⁸ The National Conference of Bankruptcy Judges submitted an alternative draft of a bill to the House as H.R. 16643.¹⁴⁹ No action was taken on either bill in the 93rd Congress, and both drafts were resubmitted in the 94th Congress as H.R. 31¹⁵⁰ and S. 235¹⁵¹ (the Commission's bill), and H.R. 32¹⁵² and S. 236¹⁵³ (the Judges' bill).¹⁵⁴ Extensive hearings were held by the respective House and Senate Judiciary Committees.¹⁵⁵

With respect to railroad bankruptcy reorganization, the recommendations of both the Bankruptcy Commission and the Judges Conference were essentially the same. Reorganization plans need not be submitted to the ICC for certification, but such plans as the court "finds worthy of consideration" would be submitted to the Commission for "examination and advisory report."¹⁵⁶ Any line abandonment, however, would require approval by the ICC. Approval could be granted expressly or by reason of ICC inaction.¹⁵⁷ After the ICC had transmitted its advice to the court, or had expressed its intent to remain silent,

145. *Id.*

146. Act of July 24, 1970, Pub. L. No. 91-354, 84 Stat. 468. The creation of the Commission was preceded by Senate investigation of the bankruptcy laws. *Hearings on S.J. Res. 100 Before the Subcomm. on Bankruptcy of the Senate Comm. on the Judiciary*, 90th Cong., 2d Sess. (1968).

147. H.R. 10792, 93d Cong., 1st Sess. (1973).

148. S. 4026, 93d Cong., 1st Sess. (1973).

149. H.R. 16643, 93d Cong., 2d Sess. (1974).

150. H.R. 31, 94th Cong., 1st Sess. (1975). *See also Hearings on H.R. 31 and H.R. 32 Before the Subcomm. on Civil and Constitutional Rights of the House Comm. on the Judiciary*, 94th Cong., 1st and 2d Sess., appendix (1975-1976) [hereinafter cited as *1975-1976 Hearings*].

151. S. 235, 94th Cong., 1st Sess. (1974).

152. H.R. 32, 94th Cong., 1st Sess. (1974). *See also 1975-1976 Hearings, supra* note 151.

153. S. 236, 94th Cong., 1st Sess. (1974).

154. *See* H.R. REP. NO. 95-595, 95th Cong., 2d Sess. 2-3 (1978), *reprinted in* [1978, No. 11c] U.S. CODE CONG. & AD. NEWS 179-81; S. REP. NO. 95-989, 95th Cong., 2d Sess. 1-2 (1978), *reprinted in* [1978, No. 11c] U.S. CODE CONG. & AD. NEWS 3-4.

155. *1975-1976 Hearings, supra* note 150; *Hearings on S. 235 and S. 236 Before the Subcomm. on Improvements in Judicial Machinery of the Senate Comm. on the Judiciary*, 94th Cong., 1st Sess. (1975).

156. H.R. 31, 94th Cong., 1st Sess. § 9-503(a) (1974) [hereinafter cited as H.R. 31]; H.R. 32, 94th Cong., 1st Sess. § 10-503(a) (1974) [hereinafter cited as H.R. 32]; *1975-1976 Hearings, supra* note 150, at 318-19.

157. H.R. 31, *supra* note 156, § 9-403(a); H.R. 32, *supra* note 156, § 10-403(a); *1975-1976 Hearings, supra* note 150, at 316-17.

the court would notice a hearing of all creditor and stockholder objections to the reorganization plan,¹⁵⁸ following which the court would submit the plan for creditor approval.¹⁵⁹ If a simple majority (measured by dollar volume of claims actually voting) of each class of creditors approved the plan,¹⁶⁰ then the court would confirm the plan provided, *inter alia*, that it was "compatible with the public interest."¹⁶¹ If a class of creditors or equity security holders rejected the plan, then the plan itself would have to provide for payment of the value of the claims.¹⁶²

This procedure differed from the existing law in several respects: (1) it eliminated the need for court "approval" of the plan prior to confirmation,¹⁶³ (2) it required creditor acceptance by simple rather than two-thirds majority,¹⁶⁴ (3) it provided for cash payment of the value of claims of creditors who had rejected the plan rather than testing creditor rejection against some standard of reasonableness,¹⁶⁵ and (4) it vested in the court, rather than the ICC, the decision as to whether the plan was or was not compatible with the public interest.¹⁶⁶

With respect to the takings problem developed in this note, these changes are fundamental. First, since joint approval of a plan was not necessary, the time-consuming process of review and resubmission by both the ICC and the bankruptcy court would be eliminated. This might have provided for a speedier reorganization of the bankrupt railroad and fairer treatment of its creditors. Explicit time requirements for reorganization, however, were not included in either bill. Secondly, allowing the court to determine the compatibility of the plan and the public interest would have fundamentally altered the nature of court's confirmation decision. Rather than balancing the rights and interests of the various creditors and equity security holders after certification by the ICC, the court would be able to directly balance the rights and interests of the creditors as a group with the interest of the public in continued service. Thirdly, a reorganization plan could not have been imposed upon a class of creditors that had rejected the plan absent sat-

158. H.R. 31, *supra* note 156, § 9-503(b)-(c); H.R. 32, *supra* note 156, §§ 10-503(b)-(c); 1975-1976 Hearings, *supra* note 150, at 255.

159. H.R. 31, *supra* note 156, § 7-306(d); H.R. 32, *supra* note 156, § 7-305(d); 1975-1976 Hearings, *supra* note 150, at 255.

160. H.R. 31, *supra* note 156, at § 7-310(d); H.R. 32, *supra* note 156, § 7-308(d); 1975-1976 Hearings, *supra* note 150, at 260-61.

161. H.R. 31, *supra* note 156, § 9-503(d)(2); H.R. 32, *supra* note 156, § 10-503(d)(2); 1975-1976 Hearings, *supra* note 150, at 320.

162. H.R. 31, *supra* note 156, §§ 7-303(7)-(8); H.R. 32, *supra* note 156, §§ 7-301(7)-(8); 1975-1976 Hearings, *supra* note 150, at 249.

163. See 11 U.S.C. § 205(e) (1976) (amended 1978).

164. See *id.*

165. See *id.*

166. See *id.* § 205(d).

isfaction of their claims. This was a substitute for the existing scheme under which the plan could be imposed upon any rejecting class of creditors provided that such rejection was found to be unreasonable under all the circumstances.¹⁶⁷ Rather than balancing the interests of the rejecting creditors against those of the public, as in *Reconstruction Finance Corporation*, the court would have been required to find explicitly that the reorganization plan was compatible with the public interest *and* satisfied the claims of rejecting classes of creditors.¹⁶⁸

The role of the ICC, time requirements for confirmation of a plan, and treatment of rejecting classes of creditors were all subjects of revision in subsequent versions of the bankruptcy bills. The hearings before the House Subcommittee on Civil and Constitutional Rights resulted in the introduction of H.R. 6 in the 95th Congress,¹⁶⁹ and its mark-up, amendment and reintroduction in the same Congress on July 11, 1977 as H.R. 8200.¹⁷⁰ In the Senate, hearings before the Subcommittee on Improvements in the Judicial Machinery led to the introduction on November 1, 1977 of S. 2266¹⁷¹ and its reintroduction, with substantial amendments, on July 17, 1978.¹⁷² On many issues, the House and the Senate tended to take polar positions.

With respect to ICC involvement in the reorganization process, the House bill contemplated even less participation by the ICC than was incorporated in the original revision proposals. Under H.R. 8200, the Commission's involvement was limited to its normal regulatory functions,¹⁷³ except that any regulations which required the expenditure of money would have been ineffective absent court approval¹⁷⁴ and abandonment of a line would have been possible over the objections of the Commission.¹⁷⁵ At no time would it have been necessary to submit the reorganization plan to the Commission, even for advisory report. However, the ICC would have been granted standing to appear.¹⁷⁶ In

167. *See id.* § 205(e).

168. H.R. 31, *supra* note 156, §§ 7-303(7)-(8), 9-503(d)(2); H.R. 32, *supra* note 156, §§ 7-301(7)-(8), 10-503(d)(2); *1975-1976 Hearings, supra* note 150, at 249, 320.

169. H.R. 6, 95th Cong., 1st Sess. (1977).

170. H.R. 8200, 95th Cong., 1st Sess. (1977) [hereinafter cited as H.R. 8200]; *Hearings on S. 2266 and H.R. 8200 Before the Subcomm. on Improvements in Judicial Machinery of the Comm. on the Judiciary, 95th Cong., 1st Sess. 3-366 (1977)* [hereinafter cited as *1977 Hearings*].

171. S. 2266, 95th Cong., 1st Sess. (1977) [hereinafter cited as S. 2266-1]; *1977 Hearings, supra* note 170, at 3-366.

172. S. 2266, 95th Cong., 2d Sess. (1978) [hereinafter cited as S. 2266-2].

173. H.R. 8200, *supra* note 170, § 1164; *1977 Hearings, supra* note 170, at 248-49.

174. H.R. 8200, *supra* note 170, § 1164(1); *1977 Hearings, supra* note 170, at 248.

175. H.R. 8200, *supra* note 170, § 1169; *1977 Hearings, supra* note 170, at 260-61. Given the otherwise exclusive jurisdiction of the ICC over abandonment petitions, it is unlikely that a court would lightly ignore Commission opposition to any line abandonment or service termination.

176. H.R. 8200, *supra* note 170, § 1163; *1977 Hearings, supra* note 170, at 248.

contrast, S. 2266, as introduced on November 1, 1977, required the initial petition for reorganization relief to be filed with both the court and the Commission¹⁷⁷ and authorized the latter to hold its own hearings.¹⁷⁸ It also required the filing of the reorganization plan with the Commission for review, revision and approval¹⁷⁹ and authorized the Commission to grant such approval over the objections of materially and adversely affected creditors upon a finding "that the plan is fair and equitable" and that "the public interest in continued rail service . . . outweighs any adverse affect."¹⁸⁰ Under this version of the Senate bill, the ICC functioned not only as the advocate of the public interest, but also as the arbitrator of any conflict between the public interest and private rights. The second version of S. 2266, reported on July 17, 1978, reversed this approach and was more in line with the provisions of H.R. 8200. The Commission would approve only those elements of a plan that effect the transfer of any lines or operation of the debtor to another railroad.¹⁸¹ The overall approval and confirmation of the plan and any balancing of public and private interests was returned to the court.¹⁸²

With respect to time limits within which the reorganization process must be complete, the House and the Senate again took different approaches. In H.R. 8200, the debtor was required to file a reorganization plan within 120 days after the date on which the petition for reorganization relief is granted;¹⁸³ however the court was authorized to increase this period on request of any party in interest.¹⁸⁴ No limit was placed on the number or length of extensions of time in which to file a plan that may be granted to the debtor, nor did H.R. 8200 contemplate any time limit within which the court would confirm the reorganization plan. Aside from the decreased involvement by the ICC in the reorganization, there was nothing to prevent the process from being extremely lengthy, with concomitant erosion of the estate of the debtor and the security of the creditor. In contrast, S. 2266, in its first version, included time limits within which every major step in the reorganization must be completed. Within 240 days after the filing of the petition for relief, the trustee of the railroad would file a proposed reorganization plan with the Commission.¹⁸⁵ This filing date could be extended,

177. S. 2266-1, *supra* note 171, § 1164; *1977 Hearings, supra* note 170, at 247-48.

178. S. 2266-1, *supra* note 171, § 1168; *1977 Hearings, supra* note 170, at 246-48.

179. S. 2266-1, *supra* note 171, § 1172; *1977 Hearings, supra* note 170, at 252-56.

180. S. 2266-1, *supra* note 171, §§ 1173(b)(1)-(2); *1977 Hearings, supra* note 170, at 255-56.

181. S. 2266-2, *supra* note 172, at § 1171(c).

182. *Id.* §§ 1172-73.

183. H.R. 8200, *supra* note 170, § 1121(b); *1977 Hearings, supra* note 170, at 216.

184. H.R. 8200, *supra* note 170, § 1121(d); *1977 Hearings, supra* note 170, at 217.

185. S. 2266-1, *supra* note 170, § 1172(a); *1977 Hearings, supra* note 170, at 252.

but not by more than 120 days.¹⁸⁶ Within 90 days of filing, the Commission would be required to publish a plan;¹⁸⁷ within another 90 days, it would have to hold and complete hearings,¹⁸⁸ and within a third 90 days, the plan as revised would have to be submitted to the court.¹⁸⁹ These time limits could be extended by the court upon the request of the Commission;¹⁹⁰ however, the first version of S. 2266 required the Commission to submit a reorganization plan to the court within a period ending 630 days after the date of the petition for reorganization relief.¹⁹¹ Upon a finding by the court that the Commission or the trustee failed to submit plans within the statutory time period, “[the court] shall order the proceeding converted to a case under chapter 7 [liquidation] of this title.”¹⁹²

A two year time limit on railroad reorganization would have been a great boon to the industry’s creditors. The New York, New Haven and Hartford Railway was in reorganization seven years before inclusion into the Penn Central Transportation Company.¹⁹³ The Penn Central, as well as the other five conveying railroads, were in reorganization more than two years before operation was assumed by Conrail.¹⁹⁴ The Chicago, Rock Island and Pacific Railroad has now been in reorganization for almost six years.¹⁹⁵ It is understandable that the time limits imposed by the first version of S. 2266 were highly criticized by judges and trustees whose task is to transform a slow and unprofitable railroad into an efficient and profitable carrier.¹⁹⁶ Nor is it surprising that the second version of S. 2266 eliminated these time requirements; a reorganization plan had only to be filed with the court within 18 months after the date of the petition for relief, and the court was authorized to extend the period without limit upon a showing of good cause.¹⁹⁷

186. *Id.*

187. S. 2266-1, *supra* note 171, § 1172(d); *1977 Hearings, supra* note 170, at 253.

188. S. 2266-1, *supra* note 171, § 1172(e); *1977 Hearings, supra* note 170, at 253.

189. *Id.*

190. S. 2266-1, *supra* note 171, § 1172(f); *1977 Hearings, supra* note 170, at 253.

191. S. 2266-1, *supra* note 171, § 1175; *1977 Hearings, supra* note 170, at 257.

192. *Id.*

193. The New Haven petitioned for reorganization relief in July, 1961. The Penn Central merger was not consummated until 1968. MOODY’S, *supra* note 74, at 710.

194. Conrail did not begin operations until April 1, 1976. MOODY’S, *supra* note 74, at 686. *See* notes 95-103 *supra*.

195. *See* note 124 *supra*.

196. *See, e.g.*, statements of Judge McGarr, presently presiding over the reorganization of the Chicago, Rock Island & Pacific Railroad, and Mr. Manos, attorney for the carrier’s trustee. *1977 Hearings, supra* note 170, at 773-802. Mr. Manos stated: “I find it totally unrealistic to impose no time constraints on a widget manufacturer undergoing reorganization while simultaneously ordering railroads operating in the public interest to file acceptable plans within 28 months or be summarily liquidated.” *Id.* at 788. *See* note 217 *infra*.

197. S. 2266-2, *supra* note 172, § 1171(a).

Neither H.R. 8200 nor the most recent version of the Senate bill included time limits within which the reorganization must be completed. The Reform Act, however, follows the lead of the first version of S. 2266 and imposes such a limit. "[I]f a plan has not been confirmed . . . before five years after the date of the order for relief, the court shall, order the trustee to cease the debtor's operation and to collect and reduce to money all of the property of the estate" ¹⁹⁸ This is a mandatory section, stating the time period beyond which suspension of creditor rights will not be permitted. It represents a compromise between the suspension of creditor rights, permitted for a reasonable period of time and required to effect a reorganization of the railroad, and the creditor's need for a clear statement of when he can foreclose on the security of the indebtedness. Whether the statutory five-year period satisfies the constitutional test of reasonableness ¹⁹⁹ is, of course, a separate question, but one which, given past decisions, ²⁰⁰ will almost assuredly be answered in the affirmative.

With respect to creditors whose claims were impaired by the reorganization plan, the versions proposed by both the Judge's Conference and the Bankruptcy Commission required that the claim of any creditor whose class did not accept the reorganization must be satisfied to the extent that it was allowed. ²⁰¹ This approach was in sharp contrast to that of the existing Bankruptcy Act, which permitted the court to approve a reorganization over the objections of a class of materially and detrimentally affected creditors provided that its objections were unreasonable under all the circumstances. ²⁰² As noted in Section I of this note, the circumstances considered by the court include the public's interest in continued rail service. Both versions of S. 2266 rejected the approach of the initial reform drafts and retained that of the Bankruptcy Act, while being explicit as to the weight which should be afforded the public interest. The confirmation of a reorganization plan over the objections of materially and adversely affected creditors would require that "the public interest in continued rail service by the reorganized debtor . . . [outweigh] any adverse effect on the creditors and equity security holders," that the plan be "fair and equitable . . . and

198. Reform Act, *supra* note 3, § 1174.

199. See text accompanying notes 25-36 *supra*.

200. The facts of the *New Haven Inclusion Cases* reveal a reorganization in progress for more than five years and with no hope of future profitability for the carrier. The assets of the railroad had eroded to a value below the debt owed to the mortgage bondholders. Still, the Supreme Court affirmed a valuation of the carrier over the objection of the secured creditors and held that their dedication of security to the public in the form of continued deficit operation was reasonable and properly compelled. See text accompanying notes 25-36 *supra*. The Reform Act, by comparison, would have been much less detrimental to the New Haven's creditors.

201. See note 168 *supra*.

202. See 11 U.S.C. § 205 (1976) (amended 1978).

that it not discriminate unfairly against any class of creditors or equity security holders.”²⁰³ The effect of this provision would be to treat the public as a creditor with a claim for continued rail service that had priority overall actual creditors.

The Reform Act, like the House draft of the bill, adopts the contrary approach. Confirmation of the plan of reorganization requires that each class of creditors or equity security holders accept the plan or suffer no impairment.²⁰⁴

A claim is unimpaired if the plan “leaves unaltered the legal, equitable, and contractual rights” to which the holder of the claim is entitled, cures any default and compensates for damages, or provides for cash payment on the effective date of the plan for the allowed amount of any claim.²⁰⁵ Additionally, no plan may be confirmed unless each creditor or equity security holder receives under the plan property of a value greater than or equal to the liquidation value of the bankrupt as of the effective date of the plan.²⁰⁶

This provision encourages acceptance of any plan submitted by the impaired creditors. Since, absent confirmation, the most that any creditor or equity security holder will receive is his liquidation share at the end of the five-year reorganization period, any plan submitted for confirmation will almost certainly improve on that amount. There is no incentive to resist reorganization, and the court is never required to balance creditor rights with the public’s interest in being served.

The Reform Act also follows the trend to restrict ICC involvement in the reorganization process. Under this scheme the debtor/railroad remains within the regulatory jurisdiction of the Commission, with the exception that orders requiring the expenditure of funds are not effective without the approval of the court.²⁰⁷ Abandonment of a line requires the usual application to the Commission, but the court is authorized to ignore the Commission’s report.²⁰⁸ Any proposal to transfer to or permit the operation of the debtor’s lines by another railroad also requires the normal application to the ICC, but in these cases the Commission’s decision is deemed conclusive, subject only to appellate review.²⁰⁹ The Commission never need see the reorganization plan; it is neither authorized to hold hearings, nor is it required to express its opinion on the plan. The Commission is granted the right to

203. S. 2266-1, *supra* note 171, § 1173(b); 1977 *Hearings*, *supra* note 170, at 255-56; S. 2266-2, *supra* note 172, § 1173(b).

204. Reform Act, *supra* note 3, §§ 1129(a)(8), 1173(a)(1); H.R. 8200, *supra* note 170, §§ 1129(a)(8); 1173(a)(1); 1977 *Hearings*, *supra* note 170, at 231.

205. Reform Act, *supra* note 3, § 1124.

206. *Id.* § 1173(a)(2).

207. Reform Act, *supra* note 3, § 1166.

208. *Id.* § 1170.

209. *Id.* § 1172(b).

“appear and be heard on any issue,” but is denied standing to appeal any order or judgment entered in the case.²¹⁰ The protection of the public’s interest, along with the interests of the debtor, creditors and equity security holders, is specifically charged to the court.²¹¹

V. Conclusion

In summary, the Reform Act resolves many of the uncertainties involved in bankruptcy reorganization of a railroad. The dual jurisdiction by the bankruptcy court and the Interstate Commerce Commission and concomitant time-consuming shuttle of plans between the two is eliminated. The creation and confirmation of reorganization plans are the sole responsibility of the court, except in circumstances of merger and consolidation. An express time limit of five years is imposed on the reorganization process and creditors and equity security holders are guaranteed at least the liquidation value of their claims as of the effective date of the plan. No balancing of creditor interests and the public interest in continued rail service is required; no class of creditors rejecting a proposed plan need ever be found unreasonable.²¹²

The judicial discretion, which via decisions like the *New Haven Inclusion Cases* and *Reconstruction Finance Corporation* vitiated the protection afforded the rail creditor by the Fifth Amendment, have been eliminated in favor of a more mechanical statutory scheme. If within five years after the initial petition for relief a reorganization plan is proposed, the creditors and equity security holders may accept or reject the plan.²¹³ If the plan is accepted, all allowed claims are guaranteed satisfaction to at least their liquidation value as of the effective date of the plan.²¹⁴ If the plan is rejected, then the creditors are guaranteed the liquidation value of their claims through the actual liquidation of the railroad at the end of the five-year period.²¹⁵ In effect, the legislature has adopted the conclusion of prior case law that the Constitution does not prohibit the suspension of creditor’s rights for a reasonable period of time in order to effect a railroad reorganization plan. Although Congress cannot alter the Supreme Court’s interpretation of the Fifth Amendment, Congress can enact, and has enacted, a reorganization statute that, without reliance on the Constitution, goes far in safeguarding the rights of the railroad creditor.

The provision for a time limit on the reorganization process is re-

210. *Id.* § 1164.

211. *Id.* § 1165.

212. Contrast this with the fate of the creditors in *Reconstruction Fin. Corp. v. Denver & R.G.W.R.R.*, 328 U.S. 495 (1946).

213. Reform Act, *supra* note 3, §§ 1129, 1173(a)(1).

214. *Id.* § 1173(a)(2).

215. *Id.* § 1174.

ally quite remarkable. Theoretically, reorganization relief is most appropriate for the essentially profitable railroad, suffering only imbalance in its equity and debt structure. If the revenue from tariffs is sufficient to meet current operating expenses and only the fixed charges of debt caused insolvency, then reorganization of the financial structure is a reasonable form of relief. But if the carrier is suffering operating deficits, has a deteriorating physical plant and cannot compete with other carriers, reorganization becomes much more difficult. A fundamental restructuring of the railroad's competitive position in the marketplace of transportation is required, not a mere restructuring of liabilities. The Reform Act's five-year time limit on reorganization serves to separate the competitive railroad from the carrier that is terminally ill and protects the creditor from involuntary funding of a hopelessly inefficient operation.

The Reform Act provisions governing railroad reorganization do perpetuate the practice of past case law in their treatment of the railroad's creditors,²¹⁶ but with much greater protection of their interests. The value of the creditor's claims may erode during the reorganization process and his right to his security may be suspended for a reasonable period of time, but the creditor is obligated to dedicate his property to the public only to the extent that the railroad has a continuing obligation to render service; and, for the railroad in reorganization, that obligation lasts only five years.

It is 1985 and the Northern and Southern Railway is again burdened by deficit operations and a deteriorating physical plant. The carrier seeks reorganization under the Bankruptcy Reform Act of 1978. Numerous plans of reorganization are proposed, but foreseeing no future profitability for the carrier, each plan is rejected by vote of the creditors. After five years the Northern and Southern Railway is subjected to mandatory liquidation. Certain main lines are purchased intact by other profitable carriers; many branch lines are acquired by the communities which they service. The remainder is auctioned for scrap. The creditors receive the liquidation value of their security without further deterioration due to compelled deficit operation. The Northern and Southern will be reorganized no more.²¹⁷

216. See text accompanying notes 25-36 *supra*.

217. The Chicago, Rock Island & Pacific Railroad, which entered bankruptcy reorganization in 1975 for the third time this century, was recently the subject of an order of liquidation by the bankruptcy court following the court's rejection of the trustee's reorganization plan. Wall. St. J., Jan. 28, 1980, at 8, col. 1. The Rock has never enjoyed true prosperity and it is burdened with one of the least profitable of routes: a north-south line in mid-America. Its liquidation and parceling among the healthy carriers was inevitable, an example of which is the Southern Pacific's recent effort to purchase the Tucumari, New Mexico to Kansas City branch. See *Letting the Rock Go Under*, Wall. St. J., Oct. 19, 1979, at 20, col. 4.