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BANKRUPTCY - PUERTO RICO

In re Financial Oversight and Management Board

United States Court of Appeals, First Circuit - July 18, 2022 - F.4th - 2022 WL 2800724

In Title III debt restructuring proceedings brought pursuant to the Puerto Rico Oversight, Management, and Economic Stability Act (PROMESA), Financial Oversight and Management Board for Puerto Rico filed motion for confirmation of modified eighth amended proposed joint plan of adjustment for Commonwealth of Puerto Rico, Employees Retirement System of the Government of the Commonwealth of Puerto Rico and the Puerto Rico Public Buildings Authority.

Creditors objected. The United States District Court for the District of Puerto Rico overruled objections, and confirmed plan. Teachers' associations appealed and filed motions for stay pending appeal. The District Court denied stay motions. Board appealed to challenge ruling of Title III court that Fifth Amendment precluded plan from impairing prepetition claims for just compensation that arose under Takings Clause.

The Court of Appeals held that:

- Confirmation order under Title III of PROMESA could not be considered as categorically exempting takings claims from discharge as exercise of discretion;
- On issue of first impression, Fifth Amendment precluded impairment or discharge of prepetition claims for just compensation in bankruptcy under Title III of PROMESA; and
- Fifth Amendment did not permit impairment of prepetition claims for just compensation simply because claimants no longer possessed rights in taken property postpetition.

Live controversy existed over issue of otherwise valid Fifth Amendment takings claims arising prepetition could be discharged in bankruptcy proceedings under Title III of the Puerto Rico Oversight, Management, and Economic Stability Act (PROMESA) without payment of just compensation; although confirmed plan of adjustment provided for full payment of takings claims, plan expressly provided for such full payment only if Title III court's ruling on takings claims was upheld on appeal.

Confirmation order under Title III of Puerto Rico Oversight, Management, and Economic Stability Act (PROMESA) could not be considered as categorically exempting takings claims from discharge as exercise of discretion, since Title III court necessarily determined that discharging valid, prepetition takings claims for less than just compensation would violate Fifth Amendment and render plan providing for such discharge unconfirmable under PROMESA, Title III court never purported to exercise any discretionary authority in exempting takings claims from discharge, and Title III court would have to had reason for exercising its discretion in that manner and only possible reason could be that Fifth Amendment required exempting takings claims from discharge.

Fifth Amendment precluded impairment or discharge of prepetition claims for just compensation in bankruptcy under Title III of the Puerto Rico Oversight, Management, and Economic Stability Act (PROMESA).

Fifth Amendment did not permit impairment of prepetition claims for just compensation simply because claimants no longer possess rights in taken property after governmental obligor has sought bankruptcy relief.

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