Of Property Rights and the Fifth Amendment: FIRREA's Cross-Guarantee Reexamined

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OF PROPERTY RIGHTS AND THE FIFTH AMENDMENT:
FIRREA'S CROSS-GUARANTEE REEXAMINED

A law . . . that takes property from A. and gives it to B.: it is against all reason and justice, for a people to intrust a legislature with such powers; and therefore, it cannot be presumed that they have done it.¹

In recent years, the troubled economy of the United States has had an extremely adverse effect on the banking industry. Two years ago, problem banks in our nation numbered 1600,² and although the number of banks in immediate danger has declined,³ observers anticipate a continuation of bank failures into the mid-1990's.⁴ According to the Bush administration, the Federal Deposit Insurance Corporation's (FDIC) bank insurance fund, the fund designated to bail the nation out of the savings and loan crisis,⁵ will lose $6.1 billion by 1993 even if insurance premiums are doubled.⁶ The possibility of a publicly financed bailout is a real worry to a presidential administration that has repeatedly stated its intention to avoid the passage of new tax laws.⁷ With the

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3. Id.
4. Id.
7. Id. at 1.
8. Arndt, supra note 4, at 1.
9. The concern for the health of the FDIC's bank insurance fund, and especially for the taxpayers who feel threatened by the prospect of an insolvent fund, is exemplified by statements like the following, which were still being made more than a year after the passage of FIRREA:
   It is outrageous that taxpayers are being asked to pay billions of dollars to clean up the S&L mess. It would be even worse if we did not try our best to prevent a similar crisis at the FDIC. . . .
   . . . To do less would be to ignore the lessons of history and to place at risk the taxpayers and the long-term health of the American economy.
10. CONG. REC. S17,748-49 (daily ed. Oct. 2, 1990) (statement of Sen. Lautenberg). Congressional members have attributed many of the banking industry's current problems to "the Reagan administration's extremely poor oversight of the industry." Id. at S17,748. Regardless of the cause of the bank failures of the late 1980's, members of Congress are concerned about the possible effects on taxpayers. "The ultimate loser could be the
failure of many more banks on the horizon, however, American taxpayers are paying increasing attention to the crisis that has gripped financial institutions, including both banks and savings and loan institutions, across the country.  

In an attempt to recapitalize the deposit insurance funds and to tackle the threat of proliferating savings and loan failures, the Bush Administration played an instrumental role in the passage of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA). Through a number of its provisions, FIRREA restructured the system that regulates the nation’s banks. It authorized the expenditure of $164 billion to bail out ailing savings and loans and created the Office of Thrift Supervision (OTS) as “an office in the Department of the Treasury” to replace the Federal Home Loan Bank Board (FHLBB). The powers of the Director of the OTS were carefully...
enumerated and were somewhat broader than the powers of the FHLBB. Congress created the Resolution Trust Corporation (RTC) to take responsibility for liquidating failed savings and loan institutions. It also dissolved the FSLIC and replaced it with a new division of the FDIC: the Federal Deposit Insurance Corporation's savings insurance fund.

of this Act, the Federal Home Loan Bank Board and the position of Chairman of the Federal Home Loan Bank Board are abolished." FIRREA, § 401(a)(2), 103 Stat. at 354. In addition,

15. "Effective on the date of the enactment of this Act, the Federal Savings and Loan Insurance Corporation established under section 402 of the National Housing Act is abolished." Id. § 1437.

17. FIRREA created the bank insurance fund of the Federal Deposit Insurance Corporation:

(A) ESTABLISHMENT. — There is established a fund to be known as the Bank Insurance Fund.

(B) TRANSFER TO FUND. — On the date of the enactment of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, the Permanent Insurance Fund shall be dissolved and all assets and liabilities of the Per-
The FDIC's savings insurance fund would have been destined for the same grim fate as the FSLIC's fund if Congress had not provided another way to fund the bailouts of failed depository institutions. Commentators commonly refer to this alternative means of raising capital to help defray the FDIC's costs as the FDIC's "cross-guarantee" power. This power enables the FDIC to assess part of the cost of the bailout of a failed institution against "sibling" depository institutions— institutions owned by the same bank holding company that owns the failed institutions. The FDIC has repeatedly threatened to use this power to help defray its costs, especially in cases involving the failure of particularly large institutions. With the failure of the Bank of New England in January of 1991, the FDIC's threats became reality. Critics of the cross-guarantee power argue that its exercise constitutes an unconstitutional taking of property without due process of law.
Whether the cross-guarantee power is constitutional is an important question to the banking industry and to legal scholars alike. The power, although until recently not considered a central component of the Act, is crucial to the success of the FIRREA legislation. With the recent increase in failures of commercial banks, FIRREA's success has become a priority. The Act was implemented in the wake of a savings and loan crisis, but if effective, it could play a substantial role in combating what many see as an impending commercial banking crisis. Without the cross-guarantee, FIRREA would be meaningful but powerless; it would lack the economic weapons necessary to realize its potential. If the cross-guarantee power is constitutional, then FIRREA could be a solution to the FDIC's regulatory problems. If the cross-guarantee power is constitutional, then FIRREA could be a solution to the FDIC's regulatory problems. It would be able to provide the FDIC with funds in addition to the insurance premiums already assessed against banks, which have proven inadequate, and thereby avoid an otherwise inevitable loss to taxpayers.

This Note discusses the fairness and constitutionality of the cross-guarantee provision under the Fifth Amendment to the United States Constitution. The discussion focuses on the long-defunct doctrine of economic substantive due process, whose laissez-faire philosophy "has regained some of its former influence in the political and academic spheres." The Supreme Court has not used

of law; nor shall private property be taken for public use, without just compensation." U.S. CONST. amend. V. The Fifth Amendment was made applicable to the states in 1868 with the ratification of the Fourteenth Amendment, which provides, among other things, "nor shall any State deprive any person of life, liberty, or property, without due process of law." Id. amend. XIV, § 1. Because the FDIC is an agency created by the federal government, this Note discusses the issue of whether the cross-guarantee provision is an unconstitutional taking by the federal government, violative of the Fifth Amendment. See infra notes 99-100 and accompanying text (discussing the law of takings generally).

23. This Note does not depict FIRREA as a slightly flawed but otherwise perfect answer to the banking crisis. Other provisions of FIRREA beyond the scope of this Note may be ineffective because they increase the overall credit risk that savings and loan institutions pose. See, e.g., Alex M. Azar II, Note, FIRREA: Controlling Savings and Loan Association Credit Risk Through Capital Standards and Asset Restrictions, 100 YALE L.J. 149 (1990). Azar explained:

FIRREA's direct restrictions on the amount and type of assets that an S&L may hold are based upon the false premise that the relevant measure of risk is the riskiness of certain categories of assets. In fact, the proper measure of risk is the riskiness of the entire asset portfolio, considered as a whole. FIRREA's restrictions actually limit the opportunities for S&L's to diversify their asset portfolios, thus potentially increasing rather than decreasing overall credit risk.

Id. at 150.

24. For the text of the Fifth Amendment, see supra note 22.

the doctrine to strike down a law since the early part of this
century, but an examination of the history of the doctrine is
crucial to an understanding of the disastrous potential of the cross-
guarantee power. For as the story of economic substantive due
process shows, the cross-guarantee provision is merely the newest
-crack in the weathered façade of property rights, merely the latest
blow in a two hundred year long battle that has all but devastated
a once-sacred prerogative.27

This Note first examines the essence of the cross-guarantee
power: its history, its rationale, and its practical effect. The Note
then traces the development and death of the doctrine of economic
substantive due process, paying particular attention to its appli-
cation in Fifth and Fourteenth Amendment jurisprudence. The
Note also explains why the doctrine is currently in disfavor. Next,
the Note analyzes the cross-guarantee power in light of the doc-
trine, and examines the constitutionality of the provision under
current substantive due process jurisprudence. Finally, this Note
concludes that although the doctrine of economic substantive due
process is in disfavor and is unlikely to influence the rulings of
any federal court, application of its general principles could help
prevent unjust exercises of the cross-guarantee by protecting
against unwarranted intrusions upon property rights. Far from
recommending the revival of the doctrine of economic substantive
due process, this Note uses the doctrine to demonstrate the
inherent logical strengths and weaknesses of the cross-guarantee.

THE CROSS-GUARANTEE POWER

History and Purpose

The general category of financial institutions encompasses di-
iverse entities. The primary members of the class are commercial
banks; investment banks; credit unions, which are governed by

26. The heyday of the economic substantive due process doctrine is often referred to
as the "Lochner era," after the case of Lochner v. New York, 198 U.S. 45 (1905). For a
fuller discussion of Lochner, its progeny, and the Supreme Court's subsequent rejection
of Lochner, see infra notes 129-57 and accompanying text.

27. Even since the demise of substantive due process, property rights have continued
to erode. See generally MARY ANN GLENDON, RIGHTS TALK: THE IMPOVERISHMENT OF
POLITICAL DISCOURSE 28-32 (1991) (examining cases such as Hawaii Housing Auth. v.
Midkiff, 467 U.S. 229 (1984) and Poletown Neighborhood Council v. City of Detroit, 394
N.W.2d 455 (Mich. 1981), and concluding that the courts routinely subordinate property
rights to other rights).
their own separate legislation; and savings and loan institutions. Each type of financial institution serves a separate function within our economy and our society, but all are regulated on a dual basis.

Traditionally, savings and loan institutions (also referred to as “depository institutions” and “thrifts”) performed two basic functions: they provided a safe place for people to deposit their savings, and they made loans to the public, using the funds from deposits, for the purpose of building homes. Because of the limited nature of these functions, savings and loan institutions largely took the form of local businesses and remained wholly unregulated in the

28. Federal credit unions are governed by the Federal Credit Union Act, Pub. L. No. 73-467, 48 Stat. 1216 (1934) (codified at 12 U.S.C. §§ 1751-1795k (1988)). Under this Act, a federal credit union is “a cooperative association organized ... for the purpose of promoting thrift among its members and creating a source of credit for provident or productive purposes.” 12 U.S.C. § 1752(1) (1988). The Act established the National Credit Union Administration Board to manage the National Credit Union Administration, see id. § 1752a(a), which consists of three members appointed by the President “with the advice and consent of the Senate,” id. § 1752a(b). The organization of a credit union is a detailed procedure that parallels the organization of any corporation:

Any seven or more natural persons who desire to form a Federal credit union shall each subscribe either individually or collectively before some officer competent to administer oaths an organization certificate in duplicate which shall specifically state:

1. the name of the association;
2. the location of the proposed Federal credit union and the territory in which it will operate;
3. the names and addresses of the subscribers to the certificate and the number of shares subscribed by each;
4. the initial par value of the shares;
5. the proposed field of membership, specified in detail;
6. the term of the existence of the corporation, which may be perpetual; and
7. the fact that the certificate is made to enable such persons to avail themselves of the advantages of this chapter.

Id. § 1753. The certificate is then submitted to the Board for approval. In deciding whether to approve, the Board takes into account “(1) whether the organization certificate conforms to the provisions of this chapter; (2) the general character and fitness of the subscribers thereto; and (3) the economic advisability of establishing the proposed Federal credit union.” Id. § 1754.

United States for the better part of two centuries. They did not compete with commercial banks because of their limited function and appeal; they focused their attention on receiving savings deposits and on extending long-term loans. The speculation of the Roaring Twenties made thrifts extremely popular with depositors and borrowers alike, and until 1929, the savings and loan industry expanded.

Between 1930 and 1935 almost a thousand thrifts failed. After acting to stabilize the banking industry, Congress turned its attention to savings and loans. The resulting Federal Home Loan Bank Act established the Federal Home Loan Bank System, which was overseen by the Federal Home Loan Bank Board. The system created by the Act to govern the savings and loan industry was based upon and analogous to the system already in place to regulate the commercial bank industry. The Federal Home Loan Bank Act established a dual (state and federal) regulatory scheme and created the Federal Savings and Loan Insurance Corporation (FSLIC), analogous to the Federal Deposit Insurance Corporation, as the insurance administrator for insured savings and loan institutions.

With the advent of the Reagan era and the general trend toward deregulation, Congress passed legislation that largely deregulated the savings and loan industry. The legislation removed the upper

31. Id. at 15.
32. Id. at 16.
33. Id.
34. Id. at 17.
36. See id.
37. FIRREA abolished both the Federal Home Loan Bank Board and the Federal Savings and Loan Insurance Corporation and redistributed the funds and functions of these two organizations within the federal bank regulatory scheme. See supra notes 12-17 and accompanying text.
38. Professor Garten notes that traditional regulation of the commercial banking industry often took place from the perspective of a typical debtholder, who was unlikely to take large risks with investments, “preferring a steady rate of return to aggressive profit-seeking.” Helen A. Garten, Regulatory Growing Pains: A Perspective on Bank Regulation in a Deregulatory Age, 57 FORDHAM L. REV. 501, 505 (1989). This characterization of commercial banking regulation is equally apt in the field of savings and loan regulation. Indeed, as some have said of the banking industry, “‘the return of your money is more important than the return on your money.’” 136 CONG. REC. H7496 (daily ed. Sept. 12, 1990) (statement of Rep. Kleczka, quoting financier Bernard Baruch).
limits on the interest rates previously allowed by Congress\textsuperscript{41} and permitted savings and loan institutions to diversify their activities, including allowing them to offer a modified checking account and higher-yield depository accounts.\textsuperscript{42} In the late 1980's, adverse economic conditions in areas such as oil production, agriculture, and loans to developing countries affected many customers' abilities to make loan payments.\textsuperscript{43} Furthermore, the New England real estate market, which had experienced rapid growth in the early and mid-1980's, collapsed in 1989, leaving behind a glut of unoccupied office buildings and condominiums.\textsuperscript{44} Savings and loan institutions that had lost their depositors to competition from money-market accounts and commercial banking portfolios found themselves struggling, and the resultant savings and loan failures depleted the FSLIC's funds:

According to the General Accounting Office (GAO), as of mid-1985, 461 of the 3180 savings and loan institutions insured by

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of the Reagan administration. Its stated purpose was "[t]o revitalize the housing industry by strengthening the financial stability of home mortgage lending institutions and ensuring the availability of home mortgage loans." \textit{Id.}, 96 Stat. at 1469. The Act increased the power of federally insured thrift institutions to invest in government securities, loans secured by nonresidential real estate, consumer loans, personal property, and educational loans. 12 U.S.C. \textsection 1464(c) (1988). Congress has often debated whether deregulation helps or hurts the banking industry. Senator Lautenberg, for example, has argued that many of the problems of the industry are due to the Reagan administration's inept oversight of financial institutions, but he nevertheless believes that encouraging a free market approach to banking is the only way to stabilize the financial condition of the nation's banks. \textit{See} 136 \textit{Cong. Rec.} S17,748-49 (daily ed. Oct. 2, 1990) (statement of Sen. Lautenberg).\textsuperscript{41} \textit{See} 12 U.S.C. \textsection 3303 (1988) (phasing out limitations on interest rates).\textsuperscript{42} \textit{See supra note 40; see also Geoffrey P. Miller, \textit{Banking Regulation: The Future of the Dual Banking System}, 53 Brook. L. Rev. 1, 4 (1987):}

Banks and thrift institutions alike suffered a massive hemorrhage of disintermediation, as their customers became unwilling to bear the opportunity costs of holding their funds in low-yielding checking or savings accounts. The regulatory system adjusted by permitting banks to offer market-rate certificates of deposit, interest bearing transaction (NOW) accounts, and insured money market accounts. Today, the price cartel has been almost completely dismantled, aside from a few vestigial rules such as the prohibition on interest-bearing commercial checking accounts.

\begin{quote}
\textsuperscript{43} Miller, supra note 42, at 10-11.
\textsuperscript{44} Roderick Oram, \textit{New England Bank to Lift Loss Reserves by 1 Billion Pounds}, \textit{FIN. TIMES}, Dec. 16, 1989, at 10; \textit{see also Hearing, supra note 7 (statement of Robert Clarke, Comptroller of the Currency) (observing that most of the failed Bank of New England's financial woes were due to its unnaturally heavy investment in the New England real estate market, which proved unstable); Therese Poletti, \textit{OTC Column—Northeastern Bank Stocks}, \textit{REUTERS}, Dec. 15, 1989 ("Most of New England's economic problems stem from overbuilding by real estate developers. Loans to developers and construction companies are the biggest problem in many banks' loan portfolios . . . . But the problems are also heightened by the slowdown among technology companies, many of which populate the Route 128 area outside Boston.")}, available in LEXIS, Nexis Library, Finrpt File.
the federal government had liabilities in excess of assets. Paying off depositors in these insolvent institutions, according to the GAO, would cost about 17 billion dollars, an amount far in excess of the FSLIC insurance fund reserves of 6.06 billion dollars.45

Something clearly needed to be done, but Congress failed to take positive action until the end of the Reagan administration. The situation called for sweeping reform legislation, before it was too late to avoid repairing the damage with massive tax increases. The result was FIRREA.46

FIRREA was a remedial measure necessitated by a general trend toward failure in the banking system.47 Several parts of the statute set forth its purpose. The preamble calls it an Act "to reform, recapitalize, and consolidate the Federal deposit insurance system, to enhance the regulatory and enforcement powers of Federal financial institutions regulatory agencies, and for other purposes."48 The cross-guarantee power is part of the attempt to recapitalize the bank regulatory system. The deposit insurance system cannot work without the funds necessary to pay the claims of the depositors of failed financial institutions.49 Congress inserted the cross-guarantee provision in an attempt to provide an alternate means of procuring the funds needed to pay depositors' claims.

FIRREA does not limit its statement of purpose to the preamble. The text of the statute declares that its goals are "[t]o provide funds from public and private sources to deal expeditiously with

45. Miller, supra note 42, at 8.
46. See supra note 9 and accompanying text. Professor Garten observed in 1989 that "[e]veryone talks about bank failure, but, like complaints about the weather, very little seems to be done about it." Helen A. Garten, What Price Bank Failure?, 50 OHIO ST. L.J. 1159, 1159 (1989). FIRREA represented an attempt to "do something about it."
47. See supra notes 2-9 and accompanying text (discussing the savings and loan crisis in general and the fact that it necessitated the passage of reform legislation).
49. Previously, the institution's total deposits determined the insurance premiums it paid to the Bank Insurance Fund:

[A] bank's assessment base for any date shall be equal to the bank's liability for deposits (including the deposits of any other depository institution for which it has assumed liability) as reported in its report of condition for such date, plus the assessment base additions set forth in paragraph (5), and less the assessment base deductions set forth in paragraph (6).

12 U.S.C. § 1817(b)(4)(A) (1988). This system of calculating insurance premiums contrasts with risk-based insurance premiums, which take into account not only the amount of deposits in a given institution, but also the risk that the institution poses to the insuring entity. See infra notes 211-12 and accompanying text (discussing risk-based insurance premiums as an alternative fund-raising method).
failed depository institutions,” “[t]o strengthen the enforcement
powers of Federal regulators of depository institutions,” and “[t]o
strengthen the civil sanctions and criminal penalties for defrauding
or otherwise damaging depository institutions and their deposi-
tors.”50 The first of these goals is perhaps the most indicative of
the purpose of the cross-guarantee provision. “Providing funds”
from “public and private sources” is an essential element of
FIRREA. One public source, namely tax dollars, was the only
alternative resource of the FSLIC before Congress implemented
FIRREA.51 As became painfully apparent to legislators and bank-
ers alike, this source was insufficient to counteract the inadequacy
of the insurance premiums paid by insured institutions.52 In en-
acting FIRREA, Congress provided the FDIC with an alternative
insurance policy: the possibility of obtaining funding from private
sources other than bank insurance premiums. The cross-guarantee
power allows the FDIC to tap the resources available within a
corporate “family” of banks in order to fund the rescue of one of
the subsidiaries. Although this seems on its face to be a reasonable
solution, its obvious consequence is that the “sibling” institutions
may also be forced into insolvency.53 This result runs counter to
critics’ urgings that “[i]n this time of restructuring of the deposit
insurance system, there is a real need to consider the interrelated
problems of bank failure, regulatory disposition of failed banks,
and the impact of that disposition on healthy banks and their
investors.”54

The purposes of the cross-guarantee clause go deeper. Before
the passage of FIRREA, the Federal Reserve Board consistently
required bank holding companies to serve as a source of “financial
and managerial strength” to their subsidiary banks.55 This policy

50. FIRREA, § 101(8)-(10), 103 Stat. at 187.
51. A public source like tax dollars is distinguishable from the private source that had
always been available to the FSLIC: insurance premiums paid by member institutions.
See supra note 18.
52. See Miller, supra note 42, at 8-10; see also supra notes 6, 17 and accompanying text
(discussing the impending failure of the bank insurance fund).
53. See infra notes 87-89 and accompanying text (discussing the Bank of New England
N.W. failure and the assessment of Maine National Bank in order to cause Maine National
Bank to fail as well).
54. Garten, supra note 46, at 1161.
55. 12 C.F.R. § 225.4(a)(1) (1991). This section specifically provides that “[a] bank holding
company shall serve as a source of financial and managerial strength to its subsidiary
banks and shall not conduct [sic] its operations in an unsafe or unsound manner.” Id.; see
also Board of Governors of the Federal Reserve System, Policy Statement on the Responsi-
bility of Bank Holding Companies to Act as Sources of Strength to their Subsidiary Banks,
was known as the “source-of-strength” doctrine. The doctrine held
bank holding companies responsible for operating sound subsid-
riaries, and the Federal Reserve Board included in this responsi-
bility an obligation to transfer funds to subsidiaries that were in
financial trouble.56

The doctrine became a formal policy in 1983 when the Federal
Reserve Board made it part of its regulations.57 As the FDIC has
accurately observed regarding the use and enforcement of the
doctrine,

[d]uring periods when the economy was favorable and few banks
were in severe financial difficulty, there was no reason to
seriously question the implications of this doctrine. Moreover,
there was no opportunity to test whether the Fed had the
authority to force a holding company to use its resources to
offset losses in a bank subsidiary when such transfers would
have a significant adverse impact on the value of the holding
company.58

The first opportunity to test the doctrine arose in early 1987,59
when the Federal Reserve Board (the Fed) ordered a multibank
holding company to provide $1.2 million in capital for one of its
failing bank subsidiaries.60 Hawkeye Bancorporation was operating
thirty-two subsidiary banks in Iowa and was financially strained
at both the parent and subsidiary levels.61 When Hawkeye refused
to comply with the order, the Fed charged the holding company
with unsafe and unsound practices.62 The Fed later withdrew the
complaint after Hawkeye argued that agreements with creditors
of the holding company precluded such a large capital injection.63

FDIC, Mandate for Change: Restructuring the Banking Industry, [1987-1988 Transfer
with “source-of-strength” doctrine).
bank holding companies to terminate nonbanking activities or divest nonbank subsidiaries
if they “constitute[ ] a serious risk to the financial safety, soundness, or stability” of a
subsidiary bank, is beyond the scope of this Note. The question the Note addresses is
whether the Federal Reserve Board should have the right to hold a company responsible
for unsound bank subsidiaries.
57. FDIC, supra note 55, at 93,026.
58. Id.
59. Id.
60. Id.
61. Id.
62. Id.
63. Id.
Subsequently, however, the Federal Reserve Board released a draft policy statement "reaffirming that holding companies should act as a source of strength, particularly in situations where the subsidiary bank is in danger of failing."\(^{64}\)

In May of 1990, the United States Court of Appeals for the Fifth Circuit struck down the source-of-strength doctrine in *MCorp Financial, Inc. v. Board of Governors.*\(^{65}\) The Board had ordered MCorp, a bank holding company based in Texas, to "implement[ ] an acceptable capital plan that would ensure that all of MCorp's available assets are used to recapitalize the Subsidiary Banks that are suffering capital deficiencies." MCorp's subsidiary banks were suffering heavy losses from real estate and energy loans.\(^{66}\)

The court held that the Federal Reserve Board, in attempting to enforce its source-of-strength doctrine against MCorp as a holding company, had exceeded its statutory authority.\(^{67}\) The district court had issued a preliminary injunction prohibiting the Board from taking further administrative action and from forcing a reorganization of the MCorp group except through bankruptcy proceedings in which restructuring would be overseen by the court.\(^{68}\)

The Board of Governors of the Federal Reserve System appealed this order, asserting that the Board was authorized

\[\text{to issue the source of strength charges under [the Bank Holding Company Act, 12 U.S.C.] §§ 1818(b)(1) and (3), which empower it to file charges against a bank holding company which the Board believes (1) has violated or is about to violate a "law, rule or regulation"; or (2) is engaging in an "unsafe or unsound" practice.}\(^{69}\)

The Board of Governors argued that MCorp had violated the Board's regulations and policy statements by refusing to act as a

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\(^{64}\) Id.

\(^{65}\) 900 F.2d 852 (5th Cir. 1990), cert. granted, 111 S. Ct. 1101 (1991). This case was pending before the passage of FIRREA, and despite the date of the decision, legislators were aware, when they enacted FIRREA in August 1989, of the courts' hostility to the source-of-strength doctrine and of the likelihood that courts would find it unenforceable.

\(^{66}\) Id. at 853.

\(^{67}\) Id. at 864. Notably, the court did not hold the source-of-strength doctrine unconstitutional; it found merely that its enforcement in this case exceeded the Board of Governors' statutory authority.

\(^{68}\) Id. at 854. The order appears in *In re MCorp, 101 B.R. 483, 490-92 (S.D. Tex. 1989), rev'd sub nom. MCorp Fin., Inc. v. Board of Governors, 900 F.2d 852 (5th Cir. 1990), cert. granted, 111 S. Ct. 1101 (1991).*

\(^{69}\) *MCorp,* 900 F.2d at 859.
source of strength for its bank subsidiaries, and that MCorp therefore was engaging in unsafe and unsound practices.\textsuperscript{70}

The court disagreed with the Board of Governors. Citing \textit{Board of Governors v. First Lincolnwood Corp.}\textsuperscript{71} and \textit{Board of Governors v. Dimension Financial Corp.}\textsuperscript{72} the court concluded that "the primary purposes of the [Bank Holding Company Act were], to prevent the concentration of control of banking resources, and to separate banking from nonbanking enterprises."\textsuperscript{73} The Board has the authority to consider financial and managerial strength when deciding whether to grant or deny applications of holding companies, but this authority is expressly limited by case law.\textsuperscript{74} The Bank Holding Company Act "does not grant the Board authority to consider the financial and managerial soundness of the subsidiary banks after it approves the application."\textsuperscript{75}

Understandably, this decision caused considerable concern to the Federal Reserve Board with regard to the source of funding for the savings and loan crisis.\textsuperscript{76} The court decided \textit{MCorp} on the basis of statutes in place before Congress passed FIRREA; the insertion into FIRREA of the cross-guarantee power subsequently overruled the decision. The case remains useful, however, in analyzing the essence of the cross-guarantee. The source-of-strength doctrine served as the ideological predecessor of the cross-guarantee provision, and the \textit{MCorp} case, though finally decided after FIRREA's ratification, certainly played a significant role in the inclusion of the provision. The passage of FIRREA with the cross-guarantee in place insured that, in enforcing the cross-guarantee, the FDIC and the Federal Reserve Board would not be acting outside their statutory authorization, as the Fed was in the \textit{MCorp} case.

\begin{itemize}
\item \textsuperscript{70} Id.
\item \textsuperscript{71} 439 U.S. 234 (1978).
\item \textsuperscript{72} 474 U.S. 361 (1986).
\item \textsuperscript{73} \textit{MCorp}, 900 F.2d at 861. The preamble to the original Bank Holding Company Act of 1956 supports this conclusion by stating that the purpose of the Act was "[t]o define bank holding companies, control their future expansion, and require divestment of their nonbanking interests." Bank Holding Company Act of 1956, Ch. 240, 70 Stat. 133. The Act was thus restrictive in nature and was intended to remedy the damage done by the lack of regulation of banks' activities and to avert future damage to the industry.
\item \textsuperscript{74} Id.
\item \textsuperscript{75} Id. (emphasis added).
\item \textsuperscript{76} See, e.g., Michael Quint, \textit{Fed's Uncertain Power Over Banking Companies}, N.Y. Times, Aug. 3, 1990, at D11. The FDIC has not supported the Federal Reserve Board's source-of-strength policy. Id.
\end{itemize}
Practical Effect

Something akin to the cross-guarantee power, therefore, has been the policy of the Federal Reserve Board for many years. The provision in FIRREA is a reaffirmation of the authority of the Board and of the FDIC to enforce the power. The cross-guarantee's practical effect, however, allows the FDIC a great deal more power than the source-of-strength doctrine ever did.

The essence of the cross-guarantee is that a "sibling institution" (that is, one that is controlled by the same holding company as the failed institution) may be held liable for the bailout of the failed institution. The Bank Holding Company Act of 1956 defines a "bank holding company" as "any company which has control over any bank or over any company that is or becomes a bank holding company by virtue of this chapter." 77

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77. The language of FIRREA specifies that funds seized pursuant to the cross-guarantee power are to be transferred directly to the FDIC; the FDIC does not force the sibling institution to inject its failed sibling directly with capital. Rather, the "insured depository institution shall pay the amount of any liability to the Corporation . . . upon receipt of written notice by the Corporation." 12 U.S.C.S. § 1815(e)(1)(B) (Law. Co-op. Supp. 1991) (emphasis added). If the liability incurred under the provision extended to the sibling institution itself, it would be necessary to determine whether the FDIC had the power to "pierce the corporate veil" between the two sibling corporations. The law of piercing the corporate veil is complex, but the general rule is that the law will recognize the separateness of corporate entities in the absence of a showing that the corporation is a "sham" or is set up for fraudulent purposes. With a few exceptions, corporateness and the positive and negative attributes of that status will nearly always be recognized:

- If any general rule can be laid down, in the present state of authority, it is that a corporation will be looked upon as a legal entity as a general rule, and until sufficient reason to the contrary appears; but, when the notion of a legal entity is used to defeat public convenience, justify wrong, protect fraud, or defend crime, the law will regard the corporation as an association of persons.

HARRY G. HENN & JOHN R. ALEXANDER, LAWS OF CORPORATIONS AND OTHER BUSINESS ENTERPRISES 346 (1983) (quoting United States v. Milwaukee Refrigerator Transit Co., 142 F. 247, 255 (C.C.E.D. Wis. 1905)). The standard for judging whether affiliated corporations (those with parent-subsidiary or sibling relationships) will be regarded as separate entities is the same as for other corporations:

- Separate corporateness of subsidiary and other affiliated corporations will be recognized, in the absence of illegitimate purposes, where
  - (a) their respective business transactions, accounts, and records are not intermingled;
  - (b) the formalities of separate corporate procedures for each corporation are observed;
  - (c) each corporation is adequately financed as a separate unit . . . ; and
  - (d) the respective enterprises are held out to the public as separate enterprises.

Id. at 354-55. For a survey of corporate veil-piercing theory, see Michael J. Gaertner, Note, Reverse Piercing the Corporate Veil: Should Corporation Owners Have it Both Ways?, 30 Wm. & MARY L. REV. 667, 677-81 (1989).

The case of the Bank of New England illustrates vividly the practical effect of the exercise of the cross-guarantee. To date, this case is the only one in which the FDIC has exercised its cross-guarantee power. The Bank of New England was a corporation with three subsidiaries: the Bank of New England N.W., based in Massachusetts; Connecticut Bank and Trust; and the Maine National Bank. The Bank of New England N.W. had invested heavily in real estate loans, and in 1989 it began to suffer losses because of the downturn in the New England real estate market. The Office of the Comptroller of the Currency (OCC) supervised the bank closely, attempting to remedy the problems, but the bank continued to suffer losses throughout 1990. These losses severely depleted the equity capital of the bank, causing the OCC to declare the bank insolvent on January 6, 1991. The FDIC became the receiver for the bank, and the bank’s failure caused the failure of its two affiliates shortly thereafter. Although one of Bank of New England N.W.’s affiliates, Connecticut Bank and Trust, failed because it was unable to recover money it had loaned to its insolvent sibling institution, the other

a company

(A) ... directly or indirectly or acting through one or more other persons owns, controls, or has power to vote 25 per centum or more of any class of voting securities of the bank or company; (B) the company controls in any manner the election of a majority of the directors or trustees of the bank or company; or (C) the Board [of Governors] determines, after notice and opportunity for hearing, that the company directly or indirectly exercises a controlling influence over the management or policies of the bank or company.

Id. § 1841(a)(2).

79. As of this writing, none of the parties to the case has initiated litigation. If the parties do decide to pursue a civil action, the case will be very important to watch because it could be the authoritative test case in the analysis of the effectiveness and validity of the cross-guarantee.

80. Hearing, supra note 7 (statement of Robert Clarke, Comptroller of the Currency).

81. Id. Comptroller Clarke explained the particular impact of the economic downturn on all three subsidiaries of the Bank of New England:

[T]his economic downturn adversely affected virtually all New England banks, but it has been particularly damaging for the bank of New England, which aggressively pursued real estate financing during this boom. By failing to adhere to sound credit underwriting standards or to maintain a properly diversified balance sheet, the bank exposed itself to disproportionate and ultimately unsustainable losses when the real estate market collapsed.

Id.

82. Id.

83. Id.

84. Id.

85. Id.

86. Id.
affiliate, Maine National Bank, was forced to close as a direct result of the FDIC's demand for compensation under FIRREA's cross-guarantee provision. As Comptroller Clarke explained to a Congressional subcommittee three days later,

The closure of Maine was triggered by the cross guarantee provision contained in the Financial Institutions Reform, Recovery and Enforcement Act of 1989. Section 206(e) of FIRREA [codified at 12 U.S.C.S. § 1815(e) (Law. Co-op. Supp. 1991)] provides that an insured depository institution can be held liable for any loss which the FDIC anticipates incurring in connection with the default of a commonly controlled insured depository institution. The FDIC, after consulting with the OCC, demanded immediate payment by Maine of an amount equal to the FDIC's expected loss as receiver for the [Blank of New England N.W.]. When Maine responded that it was unable to cover the payment, the OCC declared it insolvent and placed it in receivership. This is the first time that the cross guarantee provision of FIRREA has been used to close a bank.87

The Chairman of the FDIC readily acknowledged that his agency deliberately used the cross-guarantee provision to fail the Maine National Bank which was otherwise in sound financial condition. This was done in order to bring all the banks under our control at one time, thereby allowing us to preserve franchise value, to stabilize the entire system and to be able to sell the entire Bank of New England holding company banks to one purchaser.88

The public policy ramifications of this use of the cross-guarantee are very serious indeed. To save money and to help offset the cost of the rescue of the Bank of New England N.W. and Connecticut Bank and Trust, the OCC and the FDIC forced an admittedly solvent institution into insolvency on the basis of their statutory authority under FIRREA. This action, although not financially necessary to the FDIC, preserved the resale value of the banks, further improving the FDIC's financial condition at the end of the transaction. Surprisingly, this exercise of the cross-guarantee power

87. Id.
88. Id. (statement of William Seidman, Chairman of the Federal Deposit Insurance Corporation).
did not capture the attention of the press, and the Maine National Bank has not yet pursued any administrative or judicial remedy.

At the time of the failure of National Bank of Washington, which was "one of the most costly in the FDIC's history," the press frequently speculated that the FDIC might use its cross-guarantee power. When the National Bank of Washington became insolvent in August of 1990, the FDIC sold most of its assets to Riggs National Bank but retained the loans that it could not sell. Washington Bancorporation, which controls the National Bank of Washington, also owns two financially healthy subsidiaries, the Washington Banks of Virginia and Maryland. According to the Washington Business Journal, the FDIC eyed these subsidiaries—worth about $10 million together—for possible exercise of the cross-guarantee. The Washington Banks of Virginia and Maryland, like the Maine National Bank, would have collapsed into insolvency if the FDIC had chosen to exercise the option. The FDIC could then have sold all three failed banks and pocketed the proceeds to help defray its cost. The advisability of causing three failures to save the FDIC money has been sharply debated in the press.

The FDIC, however, made no accusations that either the National Bank of Washington or the Bank of New England had

89. What did capture attention was the FDIC's decision to insure all deposits, even if they exceeded the statutory limit of $100,000. Id. (statement of Sen. Riegle). This was justified by the "too big to fail doctrine" or "essentiality test" often applied by the FDIC, which asks whether a bank has such a great number of uninsured deposits exceeding the statutory limit that a public panic might ensue when the bank enters receivership. Id. (statements of Sens. Riegle and Dodd). Controversy has arisen because in cases like that of the Freedom National Bank in Harlem, for example, the FDIC chose not to insure any deposits when the bank failed. Even the FDIC leadership has expressed dismay that "there [is] greater protection for bigger banks' depositors than there [is] for smaller banks' depositors." Id. (testimony of William Seidman, Chairman of the Federal Deposit Insurance Corporation).


91. Id.

92. Id.

93. Id.

94. See id.

95. See, e.g., Will 'Source of Strength' Become a Source of Shake-Up?, INSTITUTIONAL INVESTOR, Aug. 1990, at 26:

"It's an important issue because it relates to the question of structure and powers," says Karen Shaw, executive vice president at the Institute for Strategy Development, a Washington-based consulting firm. "In the [MCorp] case, it was alleged that the holding company gutted the multibank system so it could isolate its problems in a few institutions and throw those into the lap of the FDIC." For their part, most bankers insist that it remains the day-to-day responsibility of a bank holding company to maintain healthy subsidiaries.
intentionally weakened their subsidiaries. All the evidence indicates that the failures were inadvertent and due to imprudent investment decisions and downturns in the markets in which the bank systems had invested.  

The practical effect of the exercise of the cross-guarantee is therefore broad. The power allows the FDIC to seize assets from banks and merge those assets with the FDIC's own funds. FIRREA requires no showing that the exercise is financially necessary; all that is necessary is a unilateral judgment on the part of the bank regulators that it would be prudent or convenient to seize these assets. A serious question therefore arises whether the cross-guarantee constitutes a taking of private property for public use or a deprivation of property under the Fifth Amendment of the United States Constitution.

ECONOMIC SUBSTANTIVE DUE PROCESS

The Fifth Amendment: Which Clause and Which Doctrine?

The Fifth Amendment provides that "[n]o person shall be... deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation." The language is simple, but it has a rich history of interpretation that must be examined in detail to determine whether a deprivation is permissible.

The second clause of the Fifth Amendment, quoted above, is often referred to as the Takings Clause. A taking is distinct from a deprivation in several ways. First, when the government "takes" property, it takes it for public use and is required to pay just compensation. An example of a taking is a condemnation action in which the government pays a property owner the fair market value of the property being taken. This clause is stricter than the first clause of the Fifth Amendment, the Deprivations Clause, because it can apply only to private property being taken for public use. The Takings Clause requires no process; its only requirement is that the former property owner be reimbursed "justly" for the value of the property.  

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96. See supra note 81 (quoting Comptroller Clarke on the cause of the insolvency of Bank of New England).
97. See supra note 88 and accompanying text (describing the reasoning for the exercise of the power thus far).
98. U.S. CONST. amend. V; see supra note 22 (discussing the different functions of the Takings Clauses under the Fifth and Fourteenth Amendments).
99. U.S. CONST. amend. V.
100. Id.
A deprivation, on the other hand, can apply to a much broader range of interests than a taking. According to the Deprivations Clause of the Fifth Amendment, the government may deprive an individual of life (for example, by imposing the death penalty), liberty (by imprisoning a felon), or property (by imposing a fine on a misdemeanant). The deprivation may take place if and only if the individual in question has received due process of law. The concept of due process breaks down even further into two categories: procedural due process and substantive due process.

Procedural due process involves the right of the individual to have some sort of procedure to determine whether the deprivation is fair. "The core requirements of procedural due process are notice and a fair hearing," but the amount of procedural process that is "due" often depends on the interest to be protected. The requirement of procedural due process protects the individual from arbitrary government action that might harm the individual's life, liberty, or property interests.

Substantive due process, on the other hand, involves "claims alleging that government action is substantively unfair or arbitrary." In other words, some individual interests are so fundamental that no amount of process will compensate the individual for the loss; regulation in these areas will always be struck down because the amount of process provided is irrelevant to the analysis of the deprivation. Justice Scalia has explained the difference between procedural due process and substantive due process:

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101. Id.
103. For example, a criminal trial in which the penalty to be imposed is a fine is likely to differ in many substantial respects from a criminal trial in which the penalty is death. Likewise, differences in procedure will be evident if the accused faces imprisonment, as opposed to a small fine.
105. These interests are most often privacy interests. See, e.g., Roe v. Wade, 410 U.S. 113 (1973) (striking down a criminal statute prohibiting the procurement of an abortion except when necessary to save the mother's life); Griswold v. Connecticut, 381 U.S. 479 (1965) (striking down a criminal statute prohibiting the use of contraceptives by married couples). Economic rights are not protected by the substantive due process doctrine, but, as Justice Scalia points out, "until the mid-1930s, substantive due process rights were extended not merely to what we would now term 'civil rights' - for example, the freedom to teach one's child a foreign language if one wishes - but also to a broad range of economic rights - for example, the right to work twelve hours a day if one wishes." Antonin Scalia, Economic Affairs as Human Affairs, in ECONOMIC LIBERTIES AND THE JUDICIARY 31, 33 (James A. Dorn & Henry G. Manne eds., 1987).
Although one might suppose that a reference to "process" places limitations only upon the manner in which a thing may be done, and not upon the doing of it, since at least the late 1800's the federal courts have in fact interpreted these clauses to prohibit the substance of certain governmental action, no matter what fair and legitimate procedures attend that substance. Thus, there has come to develop a judicial vocabulary which refers (seemingly redundantly) to "procedural due process" on the one hand, and (seemingly paradoxically) to "substantive due process" on the other hand.106

The cross-guarantee power does not lend itself to analysis under the Takings Clause. Although its exercise is technically a taking of private property for public use, the private property being taken consists of cash assets, for which the only just compensation would also be cash. If the FDIC were required to compensate insolvent banks for the money it took, the cross-guarantee would operate more like a loan than a seizure. Although this idea is appealing from a pure property-rights standpoint, it defeats the purpose of the cross-guarantee, which is to provide funds to the FDIC to aid it in its task of insuring deposits.

The cross-guarantee lends itself more easily to analysis under the Deprivations Clause. Under the Administrative Procedure Act, a comprehensive and lengthy appeal process is available to insolvent banks.107 Analysis of the procedural safeguards available to insolvent banks would require an inquiry into the constitutional soundness of the Administrative Procedure Act, which has been in place since 1946 in substantially its original form.108 Although procedural due process may be an interesting theory under which to analyze the constitutionality of the cross-guarantee, such an analysis would require an inquiry into the constitutionality of a law that has not been seriously criticized in more than fifty years.

The doctrine of substantive due process, however, provides a useful framework for analyzing the constitutionality of the cross-guarantee provision. As has been pointed out, courts have not applied substantive due process to economic rights since the 1930's.109 The Framers of the Constitution considered property

106. Scalia, supra note 105, at 33.
109. See supra note 105 (quoting Justice Scalia).
rights extremely important, however, and proponents of the sub-
stantive due process theory point out that

[The question arises whether judicial protection of the property
right is similarly important and appropriate for contemporary
society, which does not seem to have the same dedication to
ownership that prior generations did.... [The underlying basis
for securing property interests has not changed. A free society
cannot exist unless government is prohibited from confiscating
private property. If government can seize something owned
by a private citizen, it can exert enormous power over people. One
would be reluctant to speak, write, pray, or petition in a manner
displeasing to the authorities lest he lose what he has already
earned and possesses.110

In addition, the economic deregulation popularized during the
Reagan era and the recent apparent interest in the doctrine of
economic substantive due process111 will excuse a foray into the
workings of a long-defunct constitutional doctrine. Placing the
cross-guarantee power against the background of economic sub-
stantive due process will expose the logical strengths and weak-
nesses of the provision and will show the impact of this deprivation
on the banks that have been, and in the future will be, subject to
it.

The Birth and Heyday of the Doctrine

The actual origin of the doctrine of economic substantive due
process is hard to pinpoint, but historians agree that the Framers
of the Constitution regarded property and economic rights as
extremely important.112 The Framers may have had a heightened
consciousness of the importance of property rights because

111. See, e.g., Phillips, supra note 25, at 266 & n.7 (listing authors who have proposed
rehabilitation of the doctrine); see also Guy Miller Struve, The Less-Restrictive Alternative
Principle and Economic Due Process, 80 HARV. L. REV. 1463 (1967) (arguing that rather
than abandoning the doctrine of economic due process altogether, the courts should strike
down economic regulation if the legislatures have a less restrictive alternative).
112. Siegan is "persuaded that the Framers accepted, as part of the constitutional
government that they created, the common-law system and tradition to preserve and
protect the liberties of the people." SIEGAN, supra note 110, at 97. In addition, he points
out that according to the Framers, "the most fundamental of all rights were those which
protect individuals from death or incarceration at the will of the state, and an owner of
real or personal property from confiscation." Id. at 98. The Fifth Amendment protects
precisely these interests.
people of the constitutional period had more reason to comprehend the great harm that results when monarchs, lords, and officials deprive individuals of their lawfully acquired possessions and interfere in the lawful pursuit of commerce. An individual's right to own and use property free of governmental restraint (except for taxation) meant emancipation, independence, and autonomy.¹¹³

Whatever their reasons, early Supreme Court Justices accorded property rights an almost sacred respect. Justice Chase's opinion in *Calder v. Bull,*¹¹⁴ for example, in defining representative government as a "social compact," pointed out that

> [t]here are acts which the Federal... Legislature cannot do, without exceeding their authority. There are certain vital principles in our free Republican governments, which will determine and overrule an apparent and flagrant abuse of legislative power; as to authorize manifest injustice by positive law; or to take away that security for personal liberty, or private property, for the protection whereof the government was established.¹¹⁵

Chase went on to conclude that "[a] law that takes property from A. and gives it to B. is against all reason and justice."¹¹⁶ Finally, Chase stated that "[t]he Legislature... cannot... violate... the right of private property. To maintain that our Federal, or State Legislature possesses such powers, if they had not been expressly restrained; would, in my opinion, be a political heresy, altogether inadmissible in our free republican governments."¹¹⁷ Commentators have contended that the Ninth Amendment, which specifies that "[t]he enumeration in the Constitution, of certain rights, shall not be construed to deny or disparage others retained by the people,"¹¹⁸ is an illustration of the belief that certain natural rights exist above and beyond those rights created by law, and that government cannot intrude on those rights, even if specifically authorized to do so.¹¹⁹ This contention supports Chase's view of the regulation of economic rights.¹²⁰

¹¹³. *Id.* at 98.
¹¹⁴. 3 U.S. (3 Dall.) 386 (1798).
¹¹⁵. *Id.* at 388 (seriatim opinion of Chase, J.).
¹¹⁶. *Id.*
¹¹⁷. *Id.* at 388-89.
¹¹⁸. U.S. CONST. amend. IX.
¹²⁰. Slagen points out the interesting dichotomy that exists in the regulation of rights.
As the nation entered the nineteenth century, the idea of regulating economic interests was unpopular at best. In 1856, the Supreme Court, adhering to its policy of requiring economic due process, handed down one of the most unpopular decisions of its history: *Dred Scott v. Sandford.*121 *Dred Scott* was the infamous case that attempted to legitimize slavery in the United States; thus it is not surprising that the decision should go down in history as one of the most despised decisions of the United States Supreme Court. The Court has never expressly overruled *Dred Scott,*122 but has questioned the decision repeatedly. At least since the landmark racial equality case of *Brown v. Board of Education,*123 *Dred Scott* has fortunately been considered outdated, dead, and buried law.

*Dred Scott* is nevertheless a good example of the application of the doctrine of economic rights in the mid-nineteenth century. The case is well known for its facts and its holdings. Scott, a negro slave, claimed that because he and his family had lived with their owner in Missouri and Illinois before being sold to the defendant, Scott was a citizen of the United States and therefore a free man.124 Justice Taney, writing for the Court, phrased the issue thus:

Can a negro, whose ancestors were imported into this country, and sold as slaves, become a member of the political community formed and brought into existence by the Constitution of the United States, and as such become entitled to all the rights, and privileges, and immunities, guarantied by that instrument to the citizen?125

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In the context of First Amendment rights, government supervision is referred to as "censorship," whereas government supervision of economic rights is commonly referred to as "regulation." The connotations of these two terms "becloud the similarities" between the two distinct types of rights. SIEGAN, supra note 110, at 248.

121. 60 U.S. 393 (1856). *Dred Scott* is undoubtedly, and certainly understandably, at least partially responsible for the unpopularity of economic due process jurisprudence today.

122. The decision was, however, reversed by the ratification of the Thirteenth Amendment to the Constitution, which abolished slavery, see U.S. CONST. amend. XIII, § 1; the Fourteenth Amendment, which provides that "[a]ll persons born or naturalized in the United States, and subject to the jurisdiction thereof, are citizens of the United States and of the State wherein they reside," id. amend. XIV, § 1; and the Fifteenth Amendment, which sought to insure citizens' right to vote regardless of "race, color, or previous condition of servitude," id. amend. XV, § 1.


124. *Dred Scott,* 60 U.S. at 397-98.

125. Id. at 403.
Taney held that a slave was not a citizen, but property.\textsuperscript{128} To free Scott would have been a violation of the Fifth Amendment prohibition on the taking of property without due process of law.\textsuperscript{127} As Taney stated,

the rights of property are united with the rights of person, and placed on the same ground by the fifth amendment to the Constitution, which provides that no person shall be deprived of life, liberty, and property, without due process of law. And an act of Congress which deprives a citizen of the United States of his liberty or property, merely because he came himself or brought his property into a particular Territory of the United States, and who had committed no offence against the laws, could hardly be dignified with the name of due process of law.\textsuperscript{128}

The flaw in Taney's reasoning was his characterization of the slaveholder as a property owner and a citizen, although Scott was merely property and not a citizen. Only the slaveholder's rights concerned Taney, and he did not question whether Scott had been deprived of \textit{his} liberty without due process of law. Economic regulation notwithstanding, no one would argue today that one person's property rights should take precedence over another person's liberty interests. Such a holding is what made \textit{Dred Scott} perhaps the most unpopular case the Supreme Court ever decided.

Despite the disastrous result in \textit{Dred Scott} and the subsequent civil war and abolition of slavery, economic rights like those protected in \textit{Dred Scott} continued to enjoy favor in the Supreme Court. The doctrine of economic substantive due process reached its zenith in the period between 1897 and 1937. During this time, however, the Court applied the doctrine mainly to protect "freedom of contract" and individuals' freedom to work for a living at occupations of their own choosing, and not to takings or deprivations. A good example of twentieth-century application of the doctrine is the well-known and frequently-cited 1905 case of \textit{Lochner v. New York}.\textsuperscript{129}

\textit{Lochner} dealt with a New York statute regulating the hours and working conditions of persons employed in bakeries. The statute limited the hours of such employees to no more than

\begin{itemize}
\item \textsuperscript{126} Id. at 451-52.
\item \textsuperscript{127} Id. at 450.
\item \textsuperscript{128} Id.
\item \textsuperscript{129} 198 U.S. 45 (1905).
\end{itemize}
sixty hours per week, or ten hours per day. The defendant in the case ran a bakery in Utica, New York and permitted his employees to work in excess of the maximum statutorily prescribed hours. He was convicted twice of violating the statute. He appealed his second conviction, claiming that the statute was "not a reasonable exercise of the police power" and that although the statute was purportedly a health regulation, its effect was to restrict bakers' rights to work the hours of their own choosing.

The Supreme Court agreed and reversed the conviction. In a five-to-four decision, it held that the statute interfered "with the right of contract between the employer and employés, concerning the number of hours in which the latter may labor in the bakery of the employer." Under the Fourteenth Amendment, the states could impose regulations that were clearly within their police powers, like legitimate public health laws. But "[t]here is no reasonable ground for interfering with the liberty of person or the right of free contract, by determining the hours of labor, in the occupation of a baker.... We think the limit of the police power has been reached and passed in this case." The effect of the law in *Lochner* was to regulate an individual's freedom to sell or purchase labor, and the Court found this effect violative of the Constitution.

*Lochner*’s focus was on the freedom of the individual to control his own ability to enter into employment contracts, regardless of whether he was "selling" or "buying" labor. Under *Lochner*, any regulation that had the effect of impairing the freedom of contract and did not have a legitimate connection to the state's police power would be invalid under the Fourteenth Amendment. Arbitrary though it was, however, *Lochner*’s test was not an empty formality. For even though the Court struck down much regulation simply because it interfered with an individual's eco-

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130. Id. at 46 n.1.
131. Id. at 46.
132. Id. at 49.
133. Id. at 51.
134. Justice Peckham wrote the majority opinion; Justices Harlan, White, and Day dissented; and Justice Holmes filed a separate dissenting opinion.
136. *Lochner* presented a Fourteenth Amendment issue because it involved a challenge to a state statute; FIRREA's cross-guarantee presents Fifth Amendment issues because FIRREA is a federal statute. See supra note 22 and accompanying text (explaining the difference between the Fifth and Fourteenth Amendments).
138. Id. at 64.
nomic life or with ownership of property, laws with legitimate purposes sometimes withstood constitutional muster.\textsuperscript{139} The distinction between legitimate and illegitimate purposes was unacceptably vague,\textsuperscript{140} but the Court’s message was clear: property rights possessed a strength and vitality grounded in the Constitution, and legislatures could not abridge them without good reason.

The doctrine of substantive due process, however, was rushing headlong toward its own demise. As one commentator has pointed out,

[the] concept was ultimately doomed in part because under it some welfare legislation was declared unconstitutional. Probably no group of justices has ever been the object of so much criticism as have been these early proponents of substantive due process. Yet these justices sought to uphold economic liberties as much as civil libertarians strive to uphold intellectual and political rights, and... with at least as much, if not more, constitutional sanction.\textsuperscript{141}

By the end of the 1930’s, \textit{Lockner} and the concept for which it stood were completely dead, and Court has never revived the doctrine of economic substantive due process.

\textsuperscript{139} See, e.g., Village of Euclid v. Ambler Realty Co., 272 U.S. 365 (1926) (upholding a local zoning ordinance).

\textsuperscript{140} Compare \textit{Euclid} \textit{with} Pennsylvania Coal Co. v. Mahon, 260 U.S. 393 (1922). In \textit{Euclid}, the Court upheld a zoning ordinance in the face of claims that it deprived landowners “of liberty and property without due process of law” in violation of the Fourteenth Amendment. \textit{Euclid}, 272 U.S. at 384. Acknowledging lower court’s recognition that zoning laws bore “a rational relation to the health and safety of the community,” \textit{id}. at 391, the Court refused to strike down the ordinance because the plaintiff had not shown it to be “arbitrary and unreasonable, having no substantial relation to the public health, safety, morals, or general welfare,” \textit{id}. at 395.

In \textit{Mahon}, however, the Supreme Court struck down a Pennsylvania law that prevented coal companies from mining under land whenever mining might cause subsidence of land supporting homes. \textit{Mahon}, 260 U.S. at 412-13. The parties agreed that the statute “destroy[ed] previously existing rights of property and contract,” but disagreed over whether the state’s police power could be extended to protect the “public interest” in the safety of a private house. \textit{id}. at 413. The Court found this justification insufficient because the statute took the mining companies’ property without just compensation. \textit{id}. at 415-16; see also Siegan, supra note 110, at 129-31. Although \textit{Euclid} permitted states and localities to ensure that homes were exposed to “the free circulation of air” and “the rays of the sun,” \textit{Euclid}, 272 U.S. at 394, \textit{Mahon} denied them the power to keep those same homes from sliding into the ground.

In 1980, Siegan pointed out that because \textit{Mahon} did not involve contract rights, it remained the law of the land. Siegan, supra note 110, at 129. The continued validity of \textit{Mahon} is somewhat questionable following the Court’s decision in Keystone Bituminous Coal Ass’n v. DeBenedictis, 480 U.S. 470 (1987), which purported to distinguish \textit{Mahon} but came to a contrary conclusion on remarkably similar facts.

\textsuperscript{141} Bernard H. Siegan, \textit{The Supreme Court's Constitution} 42 (1987).
The Death of the Doctrine

The Great Depression led to the downfall of the doctrine of economic substantive due process. For instance, when milk prices began to decline drastically in the early 1930's, a New York State regulatory board passed minimum price legislation for milk sellers in an effort to insure that milk producers would still operate at a profit.¹⁴² The legislation criminalized the act of selling milk in a retail store for less than the statutorily prescribed price.¹⁴³ One milk seller in Rochester violated the law and was convicted; he appealed the conviction, claiming that the law infringed on his right to freedom of contract.¹⁴⁴

In *Nebbia v. New York*,¹⁴⁵ the Supreme Court began to show its uneasiness with the rule set out in *Lochner*. Justice Roberts, in framing the issue, asked "whether the Federal Constitution prohibits a state from so fixing the selling price of milk."¹⁴⁶ Uncomfortable with the prospect of overturning the conviction in the face of the milk producers' economic hardship, he explained the motivation for the legislation, remarking that "[t]he situation of the families of dairy producers had become desperate and called for state aid similar to that afforded the unemployed, if conditions should not improve."¹⁴⁷ Finally, in addressing the appellant's Fourteenth Amendment argument, Justice Roberts conceded that the freedom of contract heretofore so zealously protected was not absolute:

> Under our form of government the use of property and the making of contracts are normally matters of private and not of public concern. The general rule is that both shall be free of governmental interference. But neither property rights nor contract rights are absolute; for government cannot exist if the citizen may at will use his property to the detriment of his fellows, or exercise his freedom of contract to work them harm. Equally fundamental with the private right is that of the public to regulate it in the common interest.¹⁴⁸

*Nebbia* appeared merely to restate the Court's previous observations that legitimate purposes could permit a legislature to

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¹⁴³. *Id.*
¹⁴⁴. *Id.*
¹⁴⁶. *Id.* at 515.
¹⁴⁷. *Id.*
¹⁴⁸. *Id.* at 523 (citations omitted).
abridge property and contract rights. If one’s exercise of property or contract rights harmed another, or the public interest, the government could regulate the exercise of those rights. The Court reiterated the same formal test it had applied in previous cases: “that the end shall be accomplished by methods consistent with due process[, that the regulation] shall not be unreasonable, arbitrary or capricious, and that the means selected shall have a real and substantial relation to the object sought to be attained.” Yet property rights were no longer of paramount importance. By ranking the “common interest” and property rights as “[equally fundamental” considerations, Nebbia served as an “early warning signal of property’s shifting rank among constitutional values.”

Although Nebbia did not kill Lochner, West Coast Hotel Co. v. Parrish dealt the fatal blow. West Coast Hotel involved a chambermaid who earned a wage agreed upon when the hotel hired her. The State of Washington, however, had fixed a minimum wage for women that exceeded the chambermaid’s contractual wages. She sought recovery of the statutory wages, and the hotel responded that the minimum wage law was unconstitutional because it violated the principles of freedom of contract. The Court held that a “regulation which is reasonable in relation to its subject and is adopted in the interests of the community is due process.” The hotel, therefore, although being deprived of property, had received due process simply because the legislature had passed the law “in the interests of the community.” This broad stroke followed from the majority’s new definition of the liberty interest protected by the Fourteenth Amendment:

The Constitution does not speak of freedom of contract. It speaks of liberty and prohibits the deprivation of liberty without due process of law. In prohibiting that deprivation the Constitution does not recognize an absolute and uncontrollable liberty. Liberty in each of its phases has its history and

149. Id. at 525. Compare this language with the Court’s refusal in Village of Euclid v. Ambler Realty Co., 272 U.S. 365, 395 (1926), to strike down a zoning ordinance because the plaintiff had not shown it to be “arbitrary and unreasonable, having no substantial relation to the public health, safety, morals, or general welfare.”
150. GLENDON, supra note 27, at 27 (citing Nebbia).
151. 300 U.S. 379 (1937).
152. Id. at 388.
153. Id.
154. Id.
155. Id. at 391.
156. Id.
connotation. But the liberty safeguarded is liberty in a social organization which requires the protection of law against the evils which menace the health, safety, morals and welfare of the people.\textsuperscript{167}

In \textit{West Coast Hotel}, the Court deferred to the legislature. A legislature could make its own judgments, even if the wisdom of its action was debatable and the effects of the legislation unclear.\textsuperscript{168} This dramatic change in the law was inevitable, for the sweeping reforms of the New Deal could never have achieved their desired effect if they had been struck down on substantive due process grounds. Yet the \textit{West Coast Hotel} ruling, however sorely needed during the Depression years to enable the rise of the welfare state, nevertheless allowed those whose needs were adequately represented in the legislature to govern the property and contract rights of those who were inadequately represented. The mere fact that a legislature had passed a law meant that the person whose rights the law affected had received all the due process the Constitution required. \textit{West Coast Hotel}'s decimation of economic rights led directly to cases such as \textit{Williamson v. Lee Optical Co.},\textsuperscript{169} decided eighteen years later, in which the Court demonstrated that it "[would] not only presume that a legislature had a reasonable basis for enacting a particular economic measure, but also [would] hypothesize reasons for the law's enactment if the legislature fail[ed] to state explicitly the reasons behind its judgment."\textsuperscript{170}

\textbf{Economic Due Process Today}

Undoubtedly, the current doctrine of economic due process as exemplified in \textit{Lochner} is "dead."\textsuperscript{161} The economic jurisprudence of the \textit{Lochner} era is "now universally acknowledged to have been constitutionally improper,"\textsuperscript{162} and the Supreme Court has not used economic substantive due process reasoning to strike

\begin{footnotesize}
\begin{enumerate}
\item 167. \textit{Id.} at 391.
\item 168. \textit{Id.} at 399.
\item 169. 348 U.S. 483 (1955) (upholding a statute prohibiting opticians from fitting or duplicating eyeglasses without a prescription).
\item 160. JOHN E. NOWAK \textit{ET AL.}, \textit{CONSTITUTIONAL LAW} 446 (2d ed. 1983).
\item 162. JOHN HART ELY, DEMOCRACY AND DISTRUST: A \textsc{t}HEORY \textsc{of} \textsc{j}UDICIAL \textsc{r}EVIEW 14 (1980).
\end{enumerate}
\end{footnotesize}
FIRREA'S CROSS-GUARANTEE

down a law since 1937. Although scholars have written a great deal about the doctrine in the past twenty years, most of the comments have been negative. Some conservative scholars have recently come out in favor of reviving the doctrine, but no amount of praise is likely to convince the Supreme Court to overturn the Nebbia-West Coast Hotel line of cases and exhume a jurisprudential standard that has been dead for over half a century.

Despite this disfavor, however, “the Court has never explicitly rejected the idea that the liberty guaranteed by the fifth and fourteenth amendments includes some protection of economic rights.” The problem is that under the loose standard of West Coast Hotel v. Parrish, economic rights, particularly the right to freedom of contract, are fragile at best, and legislation affecting them does not deserve any sort of heightened scrutiny to test its validity.

Nevertheless, federal courts continue to protect quasi-economic rights on a limited basis, despite the Supreme Court's express disavowal of this sort of protection. The Court has applied substantive due process in the realm of privacy rights without hesitation; in fact, some decisions that strike down state action on the basis of privacy rights could be construed as protection of economic interests on privacy grounds. Two good examples of this sort of decision making are the recent cases of Yeager v. Hackensack Water Co. and Andrews v. Ballard.

In Yeager, the State of New Jersey had declared a drought emergency, and pursuant to an executive order, the Hackensack Water Company, which supplied water to sixty municipalities,

163. Note, supra note 119, at 1363; see West Coast Hotel v. Parrish, 300 U.S. 379 (1937).
164. See, e.g., RAUL BERGER, GOVERNMENT BY JUDICIARY: THE TRANSFORMATION OF THE FOURTEENTH AMENDMENT 265-68 (1977) (arguing that the use of substantive due process to protect personal rights is no more justified than its use to protect economic rights); Robert G. McCloskey, Economic Due Process and the Supreme Court: An Exhumation and Reburial, 1962 Sup. Ct. Rev. 34 (arguing that the Court lacks both the expertise and the power necessary to review economic legislation); Scalia, supra note 105, at 34-37 (agreeing with the Court's current position on economic rights).
165. See, e.g., Note, supra note 119, at 1363 n.1 (calling criticism of the doctrine “hostility and prejudice” and arguing for a revival of judicial protection of economic rights).
166. Id. at 1363.
167. 300 U.S. 379; see supra notes 151-57 and accompanying text (describing the standard set forth in the Court's opinion).
168. See supra, note 105 and accompanying text (describing the two uses of substantive due process: economic and privacy oriented).
began rationing water to its customers.\textsuperscript{171} The water company allowed residents to use fifty gallons of water per person per day;\textsuperscript{172} in order to assure compliance, the water company asked residents to list the names and social security numbers of all the persons living in each household.\textsuperscript{173} Failure to reply subjected the resident in question to civil and criminal sanctions.\textsuperscript{174}

The plaintiffs challenged the action on privacy grounds.\textsuperscript{175} The district court held that although Hackensack's use of social security numbers was "not per se impermissible,"\textsuperscript{176} the water company had failed to comply with the disclosure requirements of the Privacy Act of 1974.\textsuperscript{177} The court also found unconstitutional the compelled disclosure of the names of persons living within each household, because "the right to be free from compelled disclosure of the names of household members is within the right of privacy which has been recognized by the courts."\textsuperscript{178}

Although the plaintiffs in Yeager chose to base their claim on a protected right to privacy, they also sought to protect an economic interest. If they had refused to comply with the disclosure ordered by the water company, they would have been subject to criminal or civil sanctions. Under economic substantive due process doctrine, they could have challenged this potential "deprivation" under the deprivations clause of the Fourteenth Amendment.\textsuperscript{179} The plaintiffs realized, however, that their only hope for redress was assertion of their personal rights under current substantive due process doctrine. They were compelled to frame their attack within the confines of an individual-centered doctrine, for the Supreme Court no longer recognized even the tiniest vestiges of Lochner's expansive economic rights.

\textsuperscript{171} 615 F. Supp. at 1088. The court found that although the Hackensack Water Company was not actually a government agency, its actions would be treated as state actions because "[i]n certain situations, where there is a close nexus between the state and an action by a regulated entity, the action of the latter may be fairly treated as that of the state itself." \textit{Id.} at 1091 (citing Jackson v. Metropolitan Edison Co., 419 U.S. 345, 351 (1974)).

\textsuperscript{172} \textit{Id.} at 1088.

\textsuperscript{173} \textit{Id.} at 1089.

\textsuperscript{174} \textit{Id.} The criminal penalties were principally fines provided for under N.J. STAT. ANN. §§ 58:1A-16 and App. A:9-49 (West 1982).


\textsuperscript{176} \textit{Id.} at 1091.

\textsuperscript{177} \textit{Id.}

\textsuperscript{178} \textit{Id.} at 1092.

\textsuperscript{179} Of course, any state action that could result in the imposition of criminal or civil fines is potentially challengeable under the Fourteenth Amendment's Deprivations Clause; Yeager is merely an example involving privacy analysis. \textit{See supra} note 101 and accompanying text (describing the Deprivations Clause and its functions).
Like Yeager, Andrews v. Ballard was susceptible to resolution under a theory of economic rights. Andrews involved a challenge to the Texas Medical Practice Act, which provided that only licensed physicians could engage in the practice of acupuncture in the State of Texas. The plaintiffs, who sought to have the Medical Practice Act declared invalid, were not acupuncturists, but rather patients who sought acupuncture treatment. They claimed that the requirement that all acupuncturists be licensed physicians violated their Fourteenth Amendment right of privacy, because (1) their decision whether to receive medical treatment was a private one and (2) the statute, although purporting to protect public health, had the effect of nearly eliminating the practice of acupuncture in the State of Texas.

The court agreed that the regulation of the practice of acupuncture violated the plaintiffs' privacy rights under the Fourteenth Amendment. It compared the decision to receive acupuncture treatment to the decision whether to continue or terminate a pregnancy, and concluded that the decision to obtain medical treatment is, "to an extraordinary degree, intrinsically personal." The court observed that "[t]he decision can either produce or eliminate physical, psychological, and emotional ruin. It can destroy one's economic stability. It is, for some, the difference between a life of pain and a life of pleasure. It is, for others, the difference between life and death."

So the state cannot interfere with such important personal decisions even if the law in question purports to protect public health and welfare. In another era, however, the plaintiffs in Andrews might have chosen to base their claim on freedom of contract, rather than on the right to privacy. Instead of relying upon personal substantive due process, they could have chosen economic substantive due process as the basis of their claim.

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181. Id. at 1039.
182. Id. The statute had this effect because Western medicine, practiced by most licensed physicians in Texas, does not recognize the traditional Chinese medical and philosophical theory underlying the practice of acupuncture. See id. at 1043. The Board of Medical Examiners, in attempting to regulate the practice of acupuncture, called it an "experimental procedure," worthy only of practice by experienced and licensed physicians. Id. at 1041.
183. Id. at 1046-47.
184. Id. at 1047. The court distinguished the rights protected in Roe v. Wade, 410 U.S. 113 (1973) and Carey v. Population Services International, 431 U.S. 678 (1977), which may involve "other individuals," from the right to undergo medical treatment, which involves only the person seeking such treatment. Andrews, 498 F. Supp. at 1047.
They could have argued that it was their right to contract for the services of a practitioner of their own choosing, regardless of whether the particular practitioner bore the state's stamp of approval. If the court had applied a *Lochner*-like approach, this theory would have succeeded.

That a modern federal court might adopt an approach expressly disavowed by the Supreme Court is extremely unlikely, however. Any economic substantive due process claim would necessarily fail, not because patients' rights are insubstantial, but merely because the modern Court protects personal privacy rights but does not protect economic rights. Indeed, the facts of *Andrews* bear a remarkable similarity to those of *Williamson v. Lee Optical Co.*, in which the Court upheld a statute prohibiting opticians from fitting or duplicating eyeglasses without a prescription from an ophthalmologist or an optometrist. In *Williamson*, as in *Andrews*, a state prohibited a class of professionals from performing a particular medical service. In *Williamson*, however, the Court dismissed the opticians' claim with the terse declaration that "it is for the legislature, not the courts, to balance the advantages and disadvantages" of regulatory laws. How could the court have balanced those interests in *Andrews* if it lacked the power to do so in *Williamson*?

The answer is that the federal judiciary does indeed possess the power, authority, and capacity to define and protect economic rights. Although it may lack "the practical power to halt any major social developments backed by insistent popular demand," this is no justification for treating economic rights differently simply because they are economic. Indeed, courts regularly protect and uphold "quite rarified" economic interests, such as those dependent upon complex and ambiguous regulations and statutes. So although "doubts about judicial expertise and power may warrant withdrawal from some economic questions,

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186. Likewise, the practitioners could have asserted their right to engage in the occupation of their own choosing, but they would not have been successful because in such a case, the state's interest in protecting patients would be strong. An unqualified practitioner could do a great deal of harm to multiple individuals in a given locality, but a patient who is aware of the practitioner's qualifications and voluntarily seeks treatment is in danger of harming only himself. Only suits brought by patients, not by practitioners, would therefore be successful if courts adopted a *Lochner*-like approach to the question.

188. Id. at 487.
190. Scalia, *supra* note 105, at 32.
they cannot justify withdrawal from all such questions.” Oppressive and arbitrary though it was, the doctrine of economic substantive due process might have survived to the present day (albeit in a diminished form) had historical accident not led to its utter destruction. If the doctrine had survived, it might now serve a crucial function by permitting courts to protect banks from the unjust operation of FIRREA’s cross-guarantee.

THE CROSS-GUARANTEE AND ECONOMIC RIGHTS

A challenge to the cross-guarantee power would not involve assertion of the right to freedom of contract, as did challenges to the regulations in *Lochner, West Coast Hotel, and Nebbia.* Rather, the cross-guarantee constitutes a deprivation of property in the term’s most conventional sense: as Justice Chase would say, money is being taken from one party and given to another. As previously discussed, a procedural due process challenge to the cross-guarantee would probably fail because of the safeguards provided by the Administrative Procedure Act. Under the Fifth Amendment, then, the best possible argument that can be made against the cross-guarantee power involves substantive due process.

Under *West Coast Hotel* and *Williamson,* which represent the current approach to economic rights, interests such as those banks hold in their assets deserve the lowest form of protection.

191. McCloskey, supra note 164, at 53.
192. As *Nebbia* shows, the Court began a slow retreat from the *Lochner* era well before the great onslaught of New Deal legislation. See supra note 150 and accompanying text. Unfortunately, “[t]he tide of the welfare state was flowing, and no court could have reversed it.” McCloskey, supra note 164, at 53. Furthermore, in 1937 the Presidency launched a vigorous (and ultimately unsuccessful) plan to bend the Court to its will by “packing” it with six new Justices. See generally LOUIS FISHER, AMERICAN CONSTITUTIONAL LAW 1321-24 (1990) (tracing the history of the court-packing scheme). Whether these pressures influenced the Justices’ minds is impossible to know, but the fact remains that the Court soon abandoned decades of precedent and reversed itself. Rather than slowly deteriorating over many years, the doctrine of economic substantive due process was shattered in a matter of months. See id. at 1324 & n.7 (noting that *West Coast Hotel* essentially reversed a decision handed down just ten months earlier).
193. See supra notes 129-60 and accompanying text (explaining these three cases).
194. See supra notes 114-17 and accompanying text (quoting Justice Chase in *Calder v. Bull,* 3 U.S. (3 Dall.) 386, 388 (1798)). In a sense, the property is being taken for public use because the FDIC is a government agency and its function is congressionally authorized. As previously discussed, no sufficient “just compensation” for a taking of cash assets, other than a repayment of those assets, appears to exist; but a repayment would defeat the purpose of the provision altogether. See supra p. 313 and accompanying text.
195. See supra notes 107-08 and accompanying text.
The government can regulate economic interests with impunity; as long as the government accords the property owner due process, it may take the owner’s assets. Further, any “regulation which is reasonable in relation to its subject and is adopted in the interests of the community” is sufficient to satisfy the Fifth Amendment’s due process requirement.196

Modern economic substantive due process theory, if it exists, does not provide any relief to a bank aggrieved by the cross-guarantee provision. The “interest of the community” to which the cross-guarantee bears a relation is the interest of the citizens of the United States in maintaining a healthy and safe banking industry, suitable to the needs of investors and depositors. Whether the cross-guarantee is “reasonable in relation to its subject” is a closer question; a bank would have to argue that the seizure of funds from a related corporate entity is an unreasonable approach to completing the FDIC’s task as receiver of the failed financial institution. Although this argument makes sense to the disinterested layperson in view of the FDIC’s alternatives,197 the current attitude among the judiciary regarding economic rights makes it unlikely that any relief at all would be afforded an aggrieved bank. Although it seems unfair that the FDIC can make a unilateral decision to seize funds from an institution in order to buttress its own finances, an institution so assessed possesses no sound legal basis under modern Fifth Amendment jurisprudence upon which to base its claim for relief.198

Keeping in mind that the Supreme Court has not struck down an economic regulation on the basis of substantive due process since the Lochner era,199 examining the cross-guarantee under the

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197. See infra notes 210-12 and accompanying text (discussing alternative means of funding, especially risk-based insurance premiums and the unpopular possibility of increased taxation).
198. The most obviously unfair aspect of the cross-guarantee is the FDIC’s ability to use the power not only in cases of financial necessity (the cases for which the cross-guarantee was apparently meant), but in cases where it is merely convenient for the FDIC to use the power to achieve some other purpose. The exercise of the power in the Bank of New England case was not one of financial necessity, but rather one of administrative convenience. FDIC Chairman Seidman has freely acknowledged that the exercise of the power in that case was meant to render the Maine National Bank insolvent so that the FDIC could more efficiently handle the Connecticut Bank and Trust insolvency. See supra note 88 and accompanying text.
199. A good example of the Court’s consistent refusal to recognize economic substantive due process is the case of Exxon Corp. v. Governor of Maryland, 437 U.S. 117 (1978), in
doctrines of economic substantive due process (both as accepted in the early part of this century and as currently rejected) to illustrate the provision’s unfairness in operation may nevertheless be useful.

The only action required of the FDIC before assessing a commonly controlled depository institution is the service of written notice on the bank to be assessed.\(^2\) The FDIC need not show that the exercise is necessary; in fact, in the Bank of New England case, the FDIC exercised the cross-guarantee because it was convenient, not because it was financially necessary.\(^1\) The seizure of assets in this way is analogous to a pre-judicial garnishment in a civil case, because a hearing and the opportunity to appeal is available to the aggrieved bank, but only after the FDIC has ordered the payment. In *Lynch v. Household Finance Corp.*,\(^2\) a private action on a promissory note not involving a government agency,\(^2\) the plaintiff challenged a pre-judicial garnishment under 42 U.S.C. § 1983, which provides that any citizen who denies another citizen “any rights, privileges, or immunities secured by the Constitution and laws” may be liable in a civil action.\(^2\) Noting that the enjoyment of property rights was one of the primary concerns of the Framers of the Constitution,\(^2\)

which the Court upheld a Maryland law enacted during the gas shortage crisis of the early 1970's that prohibited producers or refiners from operating service stations within the state borders. The Court dismissed the appellants' substantive due process argument summarily, holding that the argument requires little discussion. The evidence presented by the refiners may cast some doubt on the wisdom of the statute, but it is, by now, absolutely clear that the Due Process Clause does not empower the judiciary "to sit as a 'superlegislature to weigh the wisdom of legislation'..." Regardless of the ultimate economic efficacy of the statute, we have no hesitancy in concluding that it bears a reasonable relation to the State's legitimate purpose in controlling the gasoline retail market.

*Id.* at 124-25 (citations omitted). The Court's unambiguous rejection of the claim leaves little room for argument.


201. *See supra* note 88 and accompanying text (quoting FDIC Chairman Seidman regarding the exercise of the cross-guarantee). Unfortunately, the FDIC's first exercise of the power was not prompted by financial necessity. Instead the FDIC undermined the policy behind the power in its initial use, calling upon the cross-guarantee to resolve administrative tangles rather than to meet a financial emergency.

202. 405 U.S. 538 (1972). *Lynch* was a procedural due process case (as opposed to a substantive due process case), but its language is relevant to the cross-guarantee because of the important status it accords property rights.

203. That neither the state nor federal government was involved in the *Lynch* case is important because of the difference governmental involvement makes in the Supreme Court's approach to such claims.

204. *Lynch*, 405 U.S. at 540 n.3. Significantly, the statute that was the basis of Mrs. Lynch's action applies only to individuals, not to governmental agencies or actors.

205. *Id.* at 544.
the Court expressly rejected the appellees' arguments that the Fourteenth Amendment and the federal statute in question protected only personal liberties and not economic rights. Economic rights therefore enjoy a protection in private civil matters at least equal to that of personal liberties; "the Congress that enacted the predecessor of [the statute in question] seems clearly to have intended to provide a federal judicial forum for the redress of wrongful deprivations of property by persons acting under color of state law."  

The approach of the *Lynch* case is an example of the fair application of the Due Process Clause of the Fourteenth Amendment. If the rationale of the case were extended both to the Fifth Amendment and to government actions like the exercise of the cross-guarantee, a fairer result would be obtained than under the alternatives currently available to aggrieved banks. Rather than making the cross-guarantee unavailable to the FDIC, a *Lynch* approach would require some sort of process before the assets could be seized. Even if the process were minimal, it would discourage the use of the cross-guarantee for the convenience of the FDIC, as in the Bank of New England case. The statute would be used for the narrow purpose for which it was intended, and achieve the results it was meant to achieve.  

A court applying substantive due process doctrine to the cross-guarantee provision might, for example, require that bank regulators make a prima facie showing of financial necessity before exercising their power. Such a requirement would apply *Nebbia*'s test to ensure that the methods used to resolve the banking crisis are not "unreasonable, arbitrary or capricious."  

206. Id. at 542.
207. Id. at 543.
208. As previously discussed, no process currently protects against an unjustified seizure of assets; the FDIC must merely inform the bank in writing that it plans to exercise the cross-guarantee. See supra note 200 and accompanying text.
209. The Supreme Court permits postdeprivation remedies to satisfy the requirement of due process if the action leading to the deprivation is random and unauthorized, if the deprivation could not have been foreseen and prevented, if a predeprivation remedy would be unfeasible, or if the state requires quick action. *Zinermon v. Burch*, 110 S. Ct. 975, 984-86 (1990). In a challenge to the cross-guarantee, the FDIC would most likely argue that the provision is justified by a need for "quick action," as one of the FDIC's primary aims is the provision of uninterrupted bank services to customers. Many bank takeovers and purchase and assumption actions occur overnight for this very reason. If the FDIC needs to provide written notice of its intent to exercise the cross-guarantee, that written notice could, with a minimal additional burden, establish a prima facie case of financial necessity. This notice requirement would bring the cross-guarantee action within the range of actions for which a postdeprivation remedy is permissible.
tion of these claims would be well within the accepted powers and capacities of the judiciary, and might even withstand appellate review so long as the court imposing the requirement avoided labeling it "substantive due process."

In the alternative, some scholars have suggested that the way around regulations that infringe on private property rights for the benefit of the public is a simple "less-restrictive alternative" test.\textsuperscript{211} "The principle is this: an economic regulation violates due process if the government has a less restrictive alternative—that is, if the government can achieve the purposes of the challenged regulation equally effectively by one or more narrower regulations."\textsuperscript{212} If raising money for the savings insurance fund is the purpose of the cross-guarantee power, several less restrictive alternatives exist. Among these options are risk-based insurance premiums, which assess individual financial institutions on a sliding scale according to the risk that they pose to their depositors. Another alternative is the slow elimination of poorly managed banks from the market by increased disclosure to the public of bank investments and management policies. Finally, the alternative of increased taxation, directed not at consumers but at bank corporations, could fatten the savings insurance fund enough to guard against depletion. A court applying the less-restrictive alternative test would strike down the cross-guarantee if it determined that one of these other alternatives could accomplish Congress' goal with equal effectiveness.

CONCLUSION

This Note shows that the doctrine of economic substantive due process, although not currently used to invalidate economic regulations, provides some useful insight into the workings and the fairness of FIRREA's cross-guarantee provision. This Note does not suggest an outright revival of the doctrine;\textsuperscript{213} such an exhumation could seriously threaten much of the social legislation that keeps our society intact. Nevertheless, if a government agency possesses unrestricted power to seize assets from a bank merely because of its relation to an insolvent financial institution,

\textsuperscript{211} See, e.g., Struve, supra note 111.

\textsuperscript{212} Id. at 1463.

\textsuperscript{213} No one would argue seriously that the era of Dred Scott, Lochner, and hour and wage regulations directed specifically toward women should be brought back to life in the 1990's.
with no process other than written notice, the possibility exists that the government may abuse its power. As illustrated by the Bank of New England scenario, the power can be used in ways for which it was not (at least not officially) intended.

More respect for the rights of sibling institutions is necessary, even if the only adjustment in FIRREA is a requirement of a prima facie showing of financial necessity along with written notice to the assessed bank. Justice Chase's ideas about property rights may be outdated in many respects, but they serve as a useful reminder of the legislature’s duties and responsibilities toward property rights, even in our modern regulated banking industry. The history of economic substantive due process shows that courts have the capacity and expertise to protect these rights.

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214. See supra note 1 and accompanying text.