UNITED STATES v. BEKINS ET AL., TRUSTEES, ET AL.

LINDSAY-STRATHMORE IRRIGATION DISTRICT v. BEKINS ET AL., TRUSTEES, ET AL.

APPEALS FROM THE DISTRICT COURT OF THE UNITED STATES FOR THE SOUTHERN DISTRICT OF CALIFORNIA.

Nos. 757 and 772. Argued April 7, 1938.—Decided April 25, 1938.

1. Proceedings for voluntary composition of debts without adjudication of bankruptcy are within the scope of the bankruptcy power. P. 47.
2. California Law, 1934, Extra Sess., gave the State's consent to the application to state "taxing districts," of the Bankruptcy Act and amendments, including Chapter X, added to that Act Aug. 16, 1937. P. 47.
3. The omission from c. X of the Bankruptcy Act of a provision specifically requiring that the petition of a state taxing district under that chapter be approved by a governmental agency of the State, *held* unimportant in determining the validity of the legislation where the State has actually consented. P. 49.
4. In conditioning the confirmation of a plan of composition upon proof that the petitioning taxing district is "authorized by law" to take all action necessary to carry out the plan, c. X of the Bankruptcy Act refers to the law of the State. P. 49.
5. Chapter X of the Bankruptcy Act, adopted Aug. 16, 1937, empowers the courts of bankruptcy to entertain and pass upon petitions by state taxing agencies or instrumentalities, including irrigation districts, for the composition of their indebtedness payable out of assessments or taxes levied against and constituting liens upon property in their districts or out of income derived therefrom or from sale of water, etc. The plan of composition must be approved by creditors owning not less than 51% of the securities affected by the plan and can not be confirmed unless accepted by creditors holding 66⅔% of the aggregate indebtedness of the district. There must be consent by the State; and the judge must be satisfied that the district is authorized by local law to carry out the plan. The statute aims to relieve serious distress existing in many such improvement districts where, because of economic conditions, property owners can not pay assessments, and taxation is useless, so that the districts can not meet

their obligations and creditors are helpless. A remedy through composition of the debts of the district could not be afforded by state law unaided, because of the contract clause of the Federal Constitution. *Held* that the statute is a valid exercise of the bankruptcy power. *Ashton* v. *Cameron County District,* 298 U. S. 513, distinguished. P. 49.

6. The ability to contract and to give consents bearing upon the exertion of governmental power is of the essence of sovereignty. P. 51.
7. The reservation to the States by the Tenth Amendment, did not destroy, but protected, their right to make contracts and give consents where that action would not contravene the provisions of the Federal Constitution. P. 52.
8. Coöperation between Nation and State through the exercise of the powers of each, to the advantage of the people who are citizens of both, is consistent with an indestructible Union of indestructible States. P. 53.
9. Chapter X of the Bankruptcy Act, *held* not violative of the Fifth Amendment, as applied to creditors of a state irrigation district, which sought a composition of its debts under that chapter. P. 54.

21 F. Supp. 129, reversed.

APPEALS from a decree of the District Court dismissing a petition for confirmation of a plan of composition presented by the above-named Irrigation District under c. X of the Bankruptcy Act. The District and the United States, which had been notified and had intervened, took separate appeals. The following arguments are extracted from a stenographic report of the hearing.

Mr. Hatton W. Sumners for the Committee on Judiciary of the House of Representatives of the United States, as *amicus curiae,* by special leave of Court.

As we understand the issues here presented, there is no question involving the rights of individuals, and there is no question with regard to the mechanics of the law. The sole question is whether or not legislation embodied in §§ 81, 82 and 83 of the Bankruptcy Act, as amended, which sections we know as the Municipal Bankruptcy Act, impinges upon the sovereignty of the State.

In this particular litigation the question arises with reference to an irrigation district.

Briefly visualizing the transactions with reference to that district and the character of the district, we observe that a group of farmers owning contiguous lands, desiring to cultivate those lands under irrigation, availed themselves of the facilities provided by the State of California for putting a blanket mortgage on those lands for the purpose of bringing water to those lands to aid them in the business of farming.

That district exercised, under delegation from the State, power of eminent domain and power of taxation. It did not relieve the State of California of any governmental responsibility theretofore exercised by it.

It seems to us that in so far as drainage and irrigation districts are concerned, they have more the characteristics of a railroad corporation than they do of an ordinary municipality. A railroad corporation, by delegation, exercises the right of eminent domain—probably as high a right and power as Government has—yet it does not thereby become a part of the State.

But I do not desire to take the time of the Court in discussing the differences, whatever they may be, between an irrigation district and an ordinary municipality, because the provisions of this Act cover them all.

When we come to examine what happened as the result of this legislation with reference to the sovereignty and dignity of the municipality, or of the State, however it may be considered, we discover that every debt which could be composed under this Act is a debt which, under the then existing law, would constitute a basis of litigation in an ordinary suit against the municipality.

The municipality, therefore, before this law was enacted, could be brought into court for these same debts by the process of the court, against the will of the municipality, the issues tried as though the municipality were

an ordinary defaulter, judgment had in the ordinary way; and if the judgment of the court were not complied with, the municipality could be brought into court again and subjected to the coercion of the court, even to the extent of the incarceration of its officers. . . .

In a similar situation this same municipality, which theretofore could be brought into court by the might of the court and without regard to its consent, under this Act comes into that court as a sovereign would come, a complete sovereign. It comes in under its own will. Nobody is compelling it to come. Nobody can compel it to come under this Act. In the exercise of its sovereign right to arrange its indebtedness—it had been sitting around a table with its creditors, and they had agreed. In the instant case 87 per cent. agreed that 59 cents on the dollar was the best thing for everybody concerned.

So this municipality, by authority of this Act, goes into that same courthouse, before the same judge, leading a procession of its consenting creditors, and says to the judge, "We have entered into this agreement, 87 per cent. There are 13 per cent. who do not consent. Will you be good enough to examine to determine whether or not this agreement is fair to the 13 per cent. and that it does not do some other things provided against in the law." It tells the court also, "I am here because, first, I was created by a sovereign State in the exercise of its sovereign powers. That sovereign gave me authority to come here. There is nowhere else myself and my creditors can go, and won't you please write our agreement into the book of judgments."

Even if it were an ordinary lawsuit, as we understand it, there is no higher act of sovereignty than for the sovereign voluntarily to submit itself to the judgment of a

court. The Federal Government does it all the time, the States do it; and we have never understood that, when a sovereign voluntarily submits itself to trial and judgment, by that submission it impairs its sovereignty or thereby makes it possible to be sued without its will.

May I respectfully submit to the Court that, instead of impinging upon the sovereignty of the State, this Act clearly is in line with the nature and philosophy of sovereignty of the State, and that to declare this Act unconstitutional would impinge upon the sovereignty of the State. Such a determination would deny to the State of California, in this matter, the right to have a sovereign will with reference to what it will permit its creatures to do.

All the way down the line there has been consent. First, the consent of the creator, California; consent of the Congress, the policy-fixing agency of the Federal Government; consent of the municipality itself, and consent of the creditors. Now, if we are to deny these agencies, which speak the voice of sovereignty and the judgment and will of the private citizen, the right thus to speak, what becomes of their sovereignty?

If the creditors consent, and the municipality consents, and the State consents, and the policy-fixing agency of the Federal Government consents, with all respect, whose else business is it, if they are sovereign?

We respectfully submit that to deny to a sovereign the right to have a sovereign will and to make that will effective, denies to it the very essence of sovereignty.

I am privileged to take a longer time of the Court, but I could not add to the substance of what I have said. We appreciate very much the Court permitting me to appear.

Solicitor General Jackson, with whom *Assistant Attorney General Whitaker,* and *Messrs. Vincent N. Miles, Warner W. Gardner,* and *Henry A. Julicher* were on the brief, for the United States in No. 757.

The District is utterly unable to meet its obligations in due course, and it is authorized by law to carry out a plan of composition.

It asks the bankruptcy court to serve the notice required by statute to bring in the dissenting creditors, to grant hearings, to hold inquiry as to the reasonableness and fairness of the plan, to stay all suits that might be brought to interfere with the District or its property meanwhile, and that the court, if it finally approves the plan, enter an order as provided for in the Act, discharging the District from all further obligations under these outstanding bonds which would be composed by a payment of 59 cents on the dollar.

The measure received careful consideration before the committees of the House and Senate, amendments were made with a view to insuring constitutionality, and the Congress concluded after full discussion that the bill as enacted was free from the objectionable features which had been held fatal to the original Act. [c. IX. See *Ashton* v. *Cameron County Dist.,* 298 U. S. 513.]

The only jurisdiction that is conferred, is the jurisdiction to compose

". . . indebtedness of or authorized by any taxing agencies or instrumentalities hereinafter named, which are payable out of assessments or taxes or both, or out of property acquired by foreclosure by the District, or out of income by such taxing districts."

These districts are then enumerated in separate subdivisions.

The purpose of the subdivisions and of the separability clause was clearly stated on the House floor by Judge Sumners.

Mr. Sumners frankly stated that the sixth classification, the political subdivisions, implied proceedings that would be unconstitutional under the *Ashton* case. He felt, however, it was not only the right, but the duty of Congress to present the question once more to this Court, since the decision, if allowed to stand, threatened grave impairment to the powers of the States, in that it forbade them to authorize their political subdivisions to enter into bankruptcy proceedings.

The case before this Court does not involve the sixth subdivision, but involves subdivision 1, so that if it be held that the law is constitutional in its application to this particular district, even though it could be held unconstitutional as applied to districts covered by subdivision 6, we are entitled to prevail.

The power to legislate on the subject of bankruptcies frequently has been passed upon by this Court. And the constitutional development of this clause at the hands of this Court in over a century has followed out the general conception of the breadth and sweep of that power as it seems to have been entertained at the time the power was given.

The whole method and purpose of bankruptcy has changed with that century of interpretation. Bankruptcy as it existed at the time, and as it existed in the first Bankruptcy Act passed by the Federal Government in 1800, was a remedy of the creditor, a further remedy, against the debtor.

It is now a new opportunity in life, and a clear field for further efforts to the bankrupt, unhampered by the pressure and discouragement of preëxisting debts. Certainly if that is the purpose of this Act, no reason appears why it should be extended to private debtors and not to public debtors. Many subdivisions of the bodies which composed the United States at the time of the Constitu-

tional Convention were themselves at that time in default, and in need, but there was no suggestion that public debtors should be excluded from the benefits of the bankruptcy power, although, we must grant, at that time the bankruptcy power was conceived to be a narrower power than it has since become.

There is equal urgency for applying this Act to public debtors—an urgency equal to any that has ever existed for extending it to private debtors.

The statistics are in the brief, and I will not dwell upon them at length, but over 2,000 improvement districts were in default in 1934. Cities as large as Detroit and Miami and Asheville were in default. 41 of the 48 States had defaults within their borders. The defaulted bonds were between one billion and two billion eight hundred million, and in 1938, when the Congress was reconsidering this matter, over 3,000 units of government were found to be in default.

The creditors in those cases stood without a practicable remedy. There is usually no property of a district subject to execution. Taxpayers are not personally liable. Mandamus to lay taxes is futile, because it results only in assessments that are defaulted. Tax sales drive down the value of property, and add further tax delinquencies. The experience of those creditors—who were themselves largely instrumental in the pressure which brought about the enactment of these Acts—the experience of those creditors was that they were without practicable remedies. This was because, though the only possible remedy was a remedy by agreement, it was almost always subject to defeat. Even though a great majority of the creditors agreed with the district on a practical course to restore some value to the defaulted bonds and to rehabilitate the district so that it could go on and exercise its public functions, any creditor who had a high estimate of the nuisance value of his particular security was in a

position to block the settlement, which required unanimous action.

Therefore the only remedy available to districts, or available to creditors, is the practicable plan of composition, in which nuisance values shall be ruled out, and in which equality of treatment of these creditors will prevail.

And it is clear that that power, as attempted to be exercised by this statute, is within the general bankruptcy power of the Congress. It is equally clear it is not within the power of the State. The States granted their power over bankruptcies to the Federal Government. They were expressly forbidden to pass laws impairing the obligation of contracts. It seems impossible to say that a statute of Congress which exercises a power twice denied to the States—denied once by delegation to the Federal Government, and denied once by express prohibition—can be an invasion of States' rights.

There is one thing the States can do. The State can connive at repudiation. It can refuse to extend remedies. It can fall back on its power to nullify a contract and refuse to approve. That, neither in point of good finance, nor of good morals, is a desirable situation. In order that the situation may be frankly faced, and that sounder remedies may be practicably applied, there must be an escape from the limitation imposed upon the State, and that escape must be found in the power of the Federal Government.

This power not only was delegated to the United States, but it was denied to the States, and it is clear the Tenth Amendment under such circumstances has no function whatever to perform in this case. Once a delegated power is found there is then no room for the operation of the Tenth Amendment.

There is then no question of state sovereignty involved, since we have a granted power.

Then there is the argument advanced here that from the necessities of our form of government, because of the dual nature of our system, there is a necessity to preserve the independence of the State and to protect its sovereignty, and that therefore this power, even though it be a delegated power, cannot be exercised if it impinges upon what would be called sovereign powers or independent powers of the State. I submit that the Tenth Amendment itself denies that argument.

If the Federal Government must point out the delegation of its powers, the Tenth Amendment equally holds the advocates of the rights of sovereignty of the States to the wording of the instrument. It clearly prohibits using the theory of necessity, the theory of the nature of government, or other philosophical reasons, for cutting down granted powers.

Now, there is an effort in the brief of our adversary to compare this power with the taxing power, and to hold that because there are certain immunities to the State and to state agencies under the taxing power, a similar immunity must be written into the bankruptcy power. That argument starts by asserting the theory that the bankruptcy power is found in the same subsection of the Constitution as the grant of the taxing power. So are the powers to regulate interstate commerce, and to punish counterfeiters. The taxing and bankruptcy powers are not parallel powers; and no argument based on the one can be applied to the other. The power of the Federal Government to tax is subject to qualification, and the bankruptcy power is not. The power to tax is to provide for the common defense and the general welfare, and hence it may very well be that where you have a plan of which the tax is a part, such as this Court held the Agricultural Adjustment Act to be, or the Child Labor Act, then you are led to an inquiry as to whether the taxing plan itself is local or is general, is national or

is within powers reserved to localities. The very nature of the taxing power, as it exists in the Federal Government, may demand that inquiry; but there is no such qualification in the bankruptcy clause. That requires only uniformity.

When we consider immunity as it exists in the States from federal taxes, and as it exists in the Government from state taxation, we are dealing with a totally different thing. The power of taxation derives from the relationship of sovereign and subject. That relationship derived originally from the duty of a sovereign to protect, and from the duty of the subject to assist the sovereign in maintaining that protection. We find no State has assumed such a duty toward the Federal Government; we find no State has assumed a relationship toward the Federal Government which in the nature of the taxing power makes it applicable, one to the other.

The very nature of the taxing power implies that it is exerted by the sovereign against the citizen, and not against another governmental body, regardless of whether the relationship is that of an equal sovereign, or that of a subsidiary governmental group.

Tax burdens, of course, are involuntary burdens and, as this Court has said, may be destructive. The power to tax may be the power to destroy, and it may be laid upon a State as a State only when it has assumed that obligation, or if the liability to taxation is to be implied from the nature of the activities of the taxpayer.

Bankruptcy is an entirely different kind of power. It is merely the opening, in this case, of a forum to which this State may resort, as we may open a forum to which foreign creditors or foreign debtors may resort.

No compulsion upon any State or State agency is here involved. This is a voluntary Act, and it raises no questions under the Eleventh Amendment.

This Court has held that, without any consent of a sovereign state, its taxing agencies may be sued. Mandamus may lie against a taxing district. And it has been held in one case that, where a state law provides a similar remedy, a receiver may be appointed to go into such a district and take over its affairs and operations.

Even the taxing immunity can be waived. This Court has held that a State may waive the tax immunity of its agencies, and that the Federal Government may waive the tax immunity of the agencies which it creates. In this case this Bankruptcy Act can never apply to any district unless there is a finding that the law of the State authorizes it to seek that remedy and authorizes it to carry that remedy to completion.

It is true we have a dual system of State and Federal Governments, but that does not mean that they can not coöperate for the common need. That question was settled by this Court in the *Social Security* cases. [301 U. S. 548, 619.]

Now, we find the State and the Nation confronted with this difficulty arising out of the limitation of the power of the State to deal with its own taxing agencies and their debts. We find these defaulted bonds in the channels of trade. We find taxing districts impaired in their capacity to carry on and perform the very functions for which they were created, and we say that there is no difficulty in the two units, the State and the Nation, without either one of them in the least receding from its sovereignty, setting up together a common remedy.

Acting Solicitor General Bell filed a memorandum for the United States in No. 757.

Messrs. Guy Knupp and *James R. McBride* for appellant in No. 772.

Mr. Knupp for the Irrigation District explained the character of the District, the history and extent of its

indebtedness and the hopelessness of its financial situation. The court below had misconceived the *Ashton* case and the nature and purpose of the new legislation. The present Act aims to avoid interference with governmental functions, public agencies, and their fiscal affairs. It deals with voluntary composition. Chapter IX gave power to the court to change the proposed plan of composition. Not so Chapter X. Chapter IX gave power to interfere with fiscal powers and policies of the public debtor. *Wright* v. *Vinton Branch,* 300 U. S. 440, is applicable.

Messrs. W. Coburn Cook and *Charles L. Childers,* with whom *Mr. Maurice E. Harrison* was on the briefs, for appellees.

Mr. Cook on behalf of appellees explained the peculiar importance of irrigation in California. The control of water is a public trust, embedded in the state constitution and executed through its laws. The work of the Irrigation District is work that the State might itself directly perform, without giving the land owners within the District any voice in the selection of managers and trustees. But California, in order that it might carry out what it conceived to be a state function, has permitted the organization of something like 100 irrigation districts in the State and has conferred upon those districts sovereign powers, the power of taxation, the power to borrow money.

The legislature itself could perform those functions directly by some department of the State. Instead of that, it chose to give the people greater control, because they were vitally interested. It could have raised revenues by direct taxation upon the entire State, because the purpose would have been public. But realizing that greater justice would be done, it allocated the indebtedness to the districts more directly affected, and thereby

permitted the people in those districts to have a voice in those affairs.

One of the greatest powers is that of borrowing money. There is a misunderstanding here as to what fiscal power is affected by this Act. It is true that in the Act everything has been done which could possibly have been thought of in order to relieve the court from the necessity of making a direct order on the district, but the effect upon the fiscal powers goes back to the time of the borrowing of the money.

Each holder of a bond and coupon is entitled to payment out of the bond values of the district in the order in which his bond or coupon has been presented. That makes each bond and coupon a separate class, and the one presented today is entitled to payment before the one presented tomorrow.

This Act would have the same effect as respects the fiscal powers of the district and State as would an exercise of powers to tax income from the bonds—it would tend much more to destroy, because under this Act you take the principal, whereas under the income act, you can take only a portion of the interest.

If this power under this Act is sustained, our great cities,—all the taxing districts, sewer districts, road districts, reclamation districts of California—could be forced into bankruptcy.

I believe it is true that a sovereign State as well as a sovereign nation does not have the right to abdicate any sovereign function which is essential to its sovereignty. *Perry* v. *United States,* 294 U. S. 330.

The Eleventh Amendment gives us no help. The State may waive its right not to be sued. The fact that these districts can be brought into court under certain conditions in no manner detracts from any essential of sovereignty, because the plaintiff in such case brought against the State is merely permitted to obtain an adju-

dication of whatever rights he may have. He is not by waiver of the immunity against suit given the right to assert other or different rights.

The Interstate Commerce Clause does not seem to us to be analogous.

I know of no principle permitting state or federal governments to waive their power to tax,—a power essential to sovereignty.

The bankruptcy power is not a power essential to the National Government. It was given to the National Government for convenience, for uniformity. It is a sort of regulatory or police power granted to the National Government, and therefore if it comes in conflict with the power of the State, which is essential to the maintenance of the sovereignty of the State, it must give way completely.

This is a bankruptcy act, whether it be called readjustment, or whether it be called composition. The effect of it is to compel certain persons to accept something which they have not contracted to accept. The difference in nomenclature between calling this district a taxing agency or a political subdivision, it seems quite obvious could have no effect upon the inherent powers which Congress may have.

Mr. Cook compared chapter X with chapter IX. One essential difference is that c. X does not require the consent of the State.

The California Enabling Act authorized the filing of a petition under c. IX.

Mr. Childers, on behalf of appellees, maintained that chapters IX and X were alike objectionable. The same classes of agencies are dealt with—arms of the sovereign power of the State. The *Ashton* case decides that the power of Congress does not extend over the sovereign function of a State.

If the power of bankruptcy extends over these state mandatories in a little way, that is, in a voluntary proceeding, it must follow that it may be exercised against these mandatories without their consent or without the consent of the State. The next logical step is to make that same power apply to the State itself. Congress must have all the power or none; and that is the principle that was announced in the *Ashton* case. We find nothing in this statute that would seem materially to differentiate it from the *Ashton* case.

To the great powers assigned to the United States by the Constitution, the States are powerless to add. Those powers are quite sufficient in themselves. The powers not delegated have been reserved to the States and to the people, and as this Court said in *United States* v. *Butler,* the Tenth Amendment was to make doubly sure.

It is the people who ultimately have the sovereign power; and the State is not in position to surrender those necessary elements of sovereignty by which it must exist.

A State, through its legislature, may consent to be sued, may surrender its sovereignty in a suit, because that is one of the powers not prohibited, and the legislature has the right to speak for the people to that extent. But it is prohibited from passing any law impairing the obligations of contract. Bankruptcy is necessarily an impairment of contract obligations. The taxing power is one of the highest attributes of sovereignty. If the United States can apply the bankruptcy power to a State, then it can control in the fiscal affairs of the State.

Though the Constitution does not expressly prohibit, State or Federal Governments may not tax each other's instrumentalities, because that would be to affect their sovereign functions. It is not a question of the size of the tax.

This must be true of bankruptcy. As soon as it touches the State in the remotest degree, it would seem that the power could not exist.

There surely cannot be a little bankruptcy. Surely Congress must have the whole power or none.

The power in bankruptcy would seem to be much more sinister than the power to tax, because the power to tax operates ordinarily in an even, like manner.

The State, of course, is prohibited by the contract clause from impairing the obligations of a contract. Now, it would seem that regardless of what sort of statute a State might pass, it can not add to or take away from the power of Congress in that regard. If a consent is needed to make an Act of Congress effective, then it must be that the power does not exist. If Congress must look to another sovereign for its power, it can not have the power.

Irrigation districts in California exercise governmental functions. The legislature has plenary power over them. They are State agencies.

The legislature can destroy them by simply repealing the Act under which they exist, and the State can go out and do the work itself, by its own agents directly. The better considered cases hold that the beneficial interest in the property acquired by one of these districts is in the State itself. It does not make much difference in this connection whether it is in the State or the land owner. The district, as a legal entity, is not the beneficial owner. If the beneficial interest is in the land owner, he must be brought into court.

How could there well be a bankruptcy of one of these public agencies that can not respond to a judgment? It has no property that is subject to execution.

In answer to questions from the Chief Justice, Mr. Childers conceded that, under chapter X, no plan of com-

position can go through unless approved by the district; and that the California Act of 1934 gave consent to the submission of such a plan under chapter IX, if not under chapter X; but he maintained that, even so, the federal bankruptcy power can not be applied.

All the power of government, whether possessed by the Nation or a State, can not be asserted to effect the composition of an indebtedness of such a district.

THE CHIEF JUSTICE. So that the State would be prohibited to effect a composition of 60 per cent., no matter how fair it is, and the Federal Government would be prohibited, although this district has an economic plight which needs relief for the benefit of the people of the district, and incidentally the people of the State. There is no power in the Government against a creditor to provide for that relief?

MR. CHILDERS. That is right. And the remedy would be much worse, I believe, than the disease.

THE CHIEF JUSTICE. Remedies often are.

MR. JUSTICE MCREYNOLDS. What power is there in a State Government or Federal Government or any other government to repudiate debts?

MR. CHILDERS. I think that is answered. I don't think there is any power, and I don't think the power ought to be there. As a matter of economics, I believe it would do much more harm to these districts than it could possibly do good. And if the power existed, the power might be exercised all the way.

By leave of Court, briefs of *amici curiae* were filed by *Messrs. U. S. Webb,* Attorney General of California, *Greek L. Rice,* Attorney General of Mississippi, *Ray McKittrick,* Attorney General of Missouri, *Gray Mashburn,* Attorney General of Nevada, *Frank H. Patton,* Attorney General of New Mexico, *I. H. Van Winkle,* Attorney General of Oregon, and *Ray E. Lee,* Attorney

General of Wyoming, on behalf of those States; *Messrs. G. W. Hamilton,* Attorney General of Washington, and *Fred J. Cunningham,* on behalf of the State of Washington; and *Messrs. Jack Holt,* Attorney General of Arkansas, and *Chas. D. Frierson,* on behalf of the State of Arkansas and certain drainage districts thereof, all in support of appellant in No. 772; by *Messrs. Cary D. Landis,* Attorney General of Florida, and *Giles J. Patterson,* on behalf of the State of Florida, in support of appellant in No. 757; and by *Messrs. Francis V. Keesling* and *Charles L. Childers,* on behalf of the West Coast Life Ins. Co., in support of appellees.

Mr. Chief Justice Hughes delivered the opinion of the Court.

These are direct appeals from the judgment of the District Court for the Southern District of California under the Act of August 24, 1937, c. 754, 50 Stat. 751. They present the question of the constitutional validity of the Act of August 16, 1937, 50 Stat. 653, amending the Bankruptcy Act by adding Chapter X providing for the composition of indebtedness of the taxing agencies or instrumentalities therein described. A certificate was issued to the Attorney General and the United States intervened. The District Court held the statute invalid as applied to the appellant and dismissed its petition for composition. The court considered itself bound by the decision in *Ashton* v. *Cameron County District,* 298 U. S. 513.

Appellant, the Lindsay-Strathmore Irrigation District, was organized in the year 1915 under the California Irrigation District Act of March 31, 1897 (Cal. Stat. 1897, p. 254). It comprises about 15,260 acres in Tulare County. It is an irrigation district and taxing agency created for the purpose of constructing and operating irrigation projects and works devoted to the improvement of lands for

agricultural purposes. On September 21, 1937, it presented its petition for the confirmation of a plan of composition. The petition alleged insolvency; that its indebtedness consisted of outstanding bonds aggregating $1,427,000 in principal, with unpaid interest of $439,085.15; that no interest or principal falling due since July 1, 1933, had been paid; that the low price of agricultural products had prevented the owners of land within the irrigation district from meeting their assessments; that upon the assessment levied by the District in the year 1932 there was a delinquency of 47 per cent. and that since that year there had been levied only an assessment of sufficient amount to maintain and operate its works; that the District's plan for the composition of its debts provided for the payment in cash of a sum equal to 59.978 cents for each dollar of the principal amount of its outstanding bonds in satisfaction of all amounts due; that creditors owning about 87 per cent. in the principal amount of the bonds had accepted the plan and consented to the filing of the petition; and that payment of the amount required was to be made from the proceeds of a loan which the Reconstruction Finance Corporation had agreed to make upon new refunding serial bonds equal to the amount borrowed and bearing interest at four per cent.

The District Court approved the petition as filed in good faith and directed the creditors to show cause why an injunction should not issue staying the commencement of suits upon the securities affected by the plan. The appellees as bondholders appeared and moved to dismiss the petition upon the ground that Chapter X of the Bankruptcy Act violated the Fifth and Tenth Amendments of the Federal Constitution. It appeared from the return to the order to show cause that these creditors had obtained an alternative writ of mandate from the state court directing the county board of supervisors to levy an assessment upon the lands within the District sufficient to pay

the amounts due the complaining creditors, and that the proceedings in that court had been suspended pending the proceeding in the bankruptcy court.

First. Chapter X of the Bankruptcy Act is limited to voluntary proceedings for the composition of debts. Aside from the question as to the power of the Congress to provide this method of relief for the described taxing agencies, it is well settled that a proceeding for composition is in its nature within the federal bankruptcy power. Compositions were authorized by the Bankruptcy Act of 1867, as amended by the Act of 1874, c. 390, § 17, 18 Stat. 182. It is unnecessary to the validity of such a proceeding that it should result in an adjudication of bankruptcy. *In re Reiman,* 20 Fed. Cas. 490, 496, 497; *Continental National Bank* v. *Chicago, R. I. & P. Ry. Co.,* 294 U. S. 648, 672, 673. In the *Continental Bank* case, in the course of a full consideration of the scope of the federal bankruptcy power and of the evolution of its exercise, we said:

"The constitutionality of the old provision for a composition is not open to doubt. *In re Reiman,* 20 Fed. Cas. 490, 496–497, cited with approval in *Hanover National Bank* v. *Moyses, supra.* [186 U. S. at p. 187.] That provision was there sustained upon the broad ground that the 'subject of bankruptcies' was nothing less than 'the subject of the relations between an insolvent or nonpaying or fraudulent debtor, and his creditors, extending to his and their relief.' That it was not necessary for the proceedings to be carried through in bankruptcy was held not to warrant the objection that the provision did not constitute a law on the subject of bankruptcies."

Second. It is unnecessary to consider the question whether Chapter X would be valid as applied to the irrigation district in the absence of the consent of the State which created it, for the State has given its consent. We think that this sufficiently appears from the statute of California enacted in 1934. Laws of 1934, Ex. Sess.,

ch. 4. This statute (§ 1) adopts the definition of "taxing districts" as described in an amendment of the Bankruptcy Act, to wit Chapter IX approved May 24, 1934, and further provides that the Bankruptcy Act and "acts amendatory and supplementary thereto, as the same may be amended from time to time, are herein referred to as the 'Federal Bankruptcy Statute'." Chapter X of the Bankruptcy Act is an amendment and appears to be embraced within the state's definition. We have not been referred to any decision to the contrary. Section 3 of the state act then provides that any taxing district in the State is authorized to file the petition mentioned in the "Federal Bankruptcy Statute." Subsequent sections empower the taxing district upon the conditions stated to consummate a plan of readjustment in the event of its confirmation by the federal court. The statute concludes with a statement of the reasons for its passage, as follows:

"There exist throughout the State of California economic conditions which make it impossible for property owners to pay their taxes and special assessments levied upon real or taxable property. The burden of such taxes and special assessments is so onerous in amount that great delinquencies have occurred in the collection thereof and seriously affect the ability of taxing districts to obtain the revenue necessary to conduct governmental functions and to pay obligations represented by bonds. It is essential that financial relief, as set forth in this act, be immediately afforded to such taxing districts in order to avoid serious impairment of their taxing systems, with consequent crippling of the local governmental functions of the State. This act will aid in accomplishing this necessary result and should therefore go into effect immediately."

While the facts thus stated related to conditions in California, similar conditions existed in other parts of the

country and it was this serious situation which led the Congress to enact Chapter IX and later Chapter X.[1]

Our attention has been called to the difference between § 80 (k) of Chapter IX and § 83 (i) of Chapter X of the Bankruptcy Act in the omission from the latter of the provision requiring the approval of the petition by a governmental agency of the State whenever such approval is necessary by virtue of the local law. We attach no importance to this omission. It is immaterial, if the consent of the State is not required to make the federal plan effective, and it is equally immaterial if the consent of the State has been given, as we think it has in this case. It should also be observed that Chapter X, § 83 (e) provides as a condition of confirmation of a plan of composition that it must appear that the petitioner "is authorized by law to take all action necessary to be taken by it to carry out the plan," and, if the judge is not satisfied on that point as well as on the others mentioned, he must enter an order dismissing the proceeding. The phrase "authorized by law" manifestly refers to the law of the State.

Third. We are thus brought to the inquiry whether the exercise of the federal bankruptcy power in dealing with a composition of the debts of the irrigation district, upon its voluntary application and with the State's consent, must be deemed to be an unconstitutional interference with the essential independence of the State as preserved by the Constitution.

In *Ashton* v. *Cameron County District, supra,* the court considered that the provisions of Chapter IX authorizing

[1] See Hearings before a Subcommittee of the Senate Committee on the Judiciary on S. 1868 and H. R. 5950, 1934, 73rd Cong., 2nd Sess.; Hearings before the House Committee on the Judiciary on H. R. 1670, etc., 1933, 73rd Cong., 1st Sess.; *Ashton* v. *Cameron County District,* 298 U. S. 513, 533, 534.

the bankruptcy court to entertain proceedings for the "readjustment of the debts" of "political subdivisions" of a State "might materially restrict its control over its fiscal affairs," and was therefore invalid; that if obligations of States or their political subdivisions might be subjected to the interference contemplated by Chapter IX, they would no longer be "free to manage their own affairs."

In enacting Chapter X the Congress was especially solicitous to afford no ground for this objection. In the report of the Committee on the Judiciary of the House of Representatives,[2] which was adopted by the Senate Committee on the Judiciary,[3] in dealing with the bill proposing to enact Chapter X, the subject was carefully considered. The Committee said:

"Compositions are approvable only when the districts or agencies file voluntary proceedings in courts of bankruptcy, accompanied by plans approved by 51 per cent of all the creditors of the district or agency, and by evidence of good faith. Each proceeding is subject to ample notice to creditors, thorough hearings, complete investigations, and appeals from interlocutory and final decrees. The plan of composition cannot be confirmed unless accepted in writing by creditors holding at least 66⅔ percent of the aggregate amount of the indebtedness of the petitioning district or taxing agency, and unless the judge is satisfied that the taxing district is authorized by law to carry out the plan, and until a specific finding by the court that the plan of composition is fair, equitable, and for the best interests of the creditors. . . .

"The Committee on the Judiciary is not unmindful of the sweeping character of the holding of the Supreme Court above referred to [in the *Ashton* case], and believes

[2] H. Rep. No. 517, 75th Cong., 1st Sess.

[3] Sen. Rep. No. 911, 75th Cong., 1st Sess.

that H. R. 5969 is not invalid or contrary to the reasoning of the majority opinion. . . .

"The bill here recommended for passage expressly avoids any restriction on the powers of the States or their arms of government in the exercise of their sovereign rights and duties. No interference with the fiscal or governmental affairs of a political subdivision is permitted. The taxing agency itself is the only instrumentality which can seek the benefits of the proposed legislation. No involuntary proceedings are allowable, and no control or jurisdiction over that property and those revenues of the petitioning agency necessary for essential governmental purposes is conferred by the bill. . . .

"There is no hope for relief through statutes enacted by the States, because the Constitution forbids the passing of State laws impairing the obligations of existing contracts. Therefore, relief must come from Congress, if at all. The committee are not prepared to admit that the situation presents a legislative no-man's land. . . . It is the opinion of the committee that the present bill removes the objections to the unconstitutional statute, and gives a forum to enable those distressed taxing agencies which desire to adjust their obligations and which are capable of reorganization, to meet their creditors under necessary judicial control and guidance and free from coercion, and to affect such adjustment on a plan determined to be mutually advantageous."

We are of the opinion that the Committee's points are well taken and that Chapter X is a valid enactment. The statute is carefully drawn so as not to impinge upon the sovereignty of the State. The State retains control of its fiscal affairs. The bankruptcy power is exercised in relation to a matter normally within its province and only in a case where the action of the taxing agency in carrying out a plan of composition approved by the bankruptcy court is authorized by state law. It is of the es-

sence of sovereignty to be able to make contracts and give consents bearing upon the exertion of governmental power. This is constantly illustrated in treaties and conventions in the international field by which governments yield their freedom of action in particular matters in order to gain the benefits which accrue from international accord. Oppenheim, International Law, 4th ed., vol. 1, §§ 493, 494; Hyde, International Law, vol. 2, § 489; *Perry* v. *United States,* 294 U. S. 330, 353; *Steward Machine Co.* v. *Davis,* 301 U. S. 548, 597. The reservation to the States by the Tenth Amendment protected, and did not destroy, their right to make contracts and give consents where that action would not contravene the provisions of the Federal Constitution. The States with the consent of Congress may enter into compacts with each other and the provisions of such compacts may limit the agreeing States in the exercise of their respective powers. Const., Art. I, § 10, subd. 3. *Poole* v. *Fleeger,* 11 Pet. 185, 209; *Rhode Island* v. *Massachusetts,* 12 Pet. 657, 725; *Hinderlider* v. *La Plata River Co., post,* p. 92. The State is free to make contracts with individuals and give consents upon which the other contracting party may rely with respect to a particular use of governmental authority. See *Fletcher* v. *Peck,* 6 Cranch 87, 137; *New Jersey* v. *Wilson,* 7 Cranch 164; *Dartmouth College* v. *Woodward,* 4 Wheat. 518, 643, 644; *Charles River Bridge* v. *Warren Bridge*, 11 Pet. 420, 549; *Jefferson Branch Bank* v. *Skelly,* 1 Black 436, 446. While the instrumentalities of the national government are immune from taxation by a State, the State may tax them if the national government consents (*Baltimore National Bank* v. *State Tax Comm'n,* 297 U. S. 209, 211, 212) and by a parity of reasoning the consent of the State could remove the obstacle to the taxation by the federal government of state agencies to which the consent applied.

Nor did the formation of an indestructible Union of indestructible States make impossible coöperation between the Nation and the States through the exercise of the power of each to the advantage of the people who are citizens of both. We had recent occasion to consider that question in the case of *Steward Machine Co.* v. *Davis, supra,* in relation to the operation of the Social Security Act of August 14, 1935. 49 Stat. 620. The question was raised with special emphasis in relation to § 904 of the statute and the parts of § 903, complementary thereto, by which the Secretary of the Treasury is authorized to receive and hold in the Unemployment Trust Fund all moneys deposited therein by a state agency for a state unemployment fund and to invest in obligations of the United States such portion of the Fund as is not in his judgment required to meet current withdrawals. The contention was that Alabama in consenting to that deposit had "renounced the plenitude of power inherent in her statehood." 301 U. S. at pp. 595, 596. We found the contention to be unsound. As the States were at liberty upon obtaining the consent of Congress to make agreements with one another, we saw no room for doubt that they may do the like with Congress if the essence of their statehood is maintained without impairment. And we added that "Nowhere in our scheme of government—in the limitations express or implied of our federal constitution—do we find that she [the State] is prohibited from assenting to conditions that will assure a fair and just requital for benefits received."

In the instant case we have coöperation to provide a remedy for a serious condition in which the States alone were unable to afford relief. Improvement districts, such as the petitioner, were in distress. Economic disaster had made it impossible for them to meet their obligations. As the owners of property within the boundaries of the district could not pay adequate assessments, the power of

taxation was useless. The creditors of the district were helpless. The natural and reasonable remedy through composition of the debts of the district was not available under state law by reason of the restriction imposed by the Federal Constitution upon the impairment of contracts by state legislation. The bankruptcy power is competent to give relief to debtors in such a plight and, if there is any obstacle to its exercise in the case of the districts organized under state law it lies in the right of the State to oppose federal interference. The State steps in to remove that obstacle. The State acts in aid, and not in derogation, of its sovereign powers. It invites the intervention of the bankruptcy power to save its agency which the State itself is powerless to rescue. Through its coöperation with the national government the needed relief is given. We see no ground for the conclusion that the Federal Constitution, in the interest of state sovereignty, has reduced both sovereigns to helplessness in such a case.

Fourth. As the bankruptcy power may be exerted to give effect to a plan for the composition of the debts of an insolvent debtor, we find no merit in appellant's objections under the Fifth Amendment. *In re Reiman, supra; Continental National Bank* v. *Chicago, R. I. & P. Ry. Co., supra.*

The judgment of the District Court is reversed and the cause is remanded for further proceedings in conformity with this opinion.

Reversed.

Mr. Justice McReynolds and Mr. Justice Butler are of the opinion that the principle approved in *Ashton* v. *Cameron County District,* 298 U. S. 513, is controlling here and requires affirmation of the questioned decree.

Mr. Justice Cardozo took no part in the consideration and decision of this case.