

## Keynote Address

# STATE DEBTS & FEDERAL JURISDICTION

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*For dryness and technicality no subject can rival public finance,  
except perhaps federal jurisdiction.<sup>1</sup>*

It is perhaps fitting to begin an article on sovereign debtors and their creditors with Ebenezer Scrooge, “a squeezing, wrenching, grasping, scraping, clutching, covetous old sinner.”<sup>2</sup> On a certain Christmas Eve in the early 1840s, the miser was visited by the ghost of his former business partner, Jacob Marley, dragging a chain made of “cash-boxes, keys, padlocks, ledgers, deeds, and heavy purses wrought in steel.”<sup>3</sup> Hoping to help Scrooge free himself from similar bondage, Marley announced that he had arranged for Scrooge to be haunted by three spirits. Although the old sinner fell asleep well after midnight, he was awakened by the sound of midnight chimes. At first, Scrooge feared that he had slept through a day on which the sun had failed to rise and that his time-sensitive securities had become worthless. When he realized that the city was not gripped by panic and that it was still the night of the same day, he heaved a great sigh of relief “because ‘three days after sight of this First of Exchange pay to Mr. Ebenezer Scrooge or his order,’ and so forth, would have become a mere United

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1. JOHN V. ORTH, *THE JUDICIAL POWER OF THE UNITED STATES: THE ELEVENTH AMENDMENT IN AMERICAN HISTORY* viii (1987).

2. CHARLES DICKENS, *A CHRISTMAS CAROL* 8 (New Oxford Illustrated Dickens 1954) (1843).

3. *Id.* at 17.

States' security if there were no days to count by.”<sup>4</sup>

Due to the reckless financiering that ended in the Panic of 1837 and the ensuing default by a number of American states, American government debt had become a byword for worthlessness. What we today would recognize as a true “United States’ security”—a treasury bill or note backed by the full faith and credit of the federal government—had not become worthless. Indeed after 1835, when the federal government paid off the first national debt in full, such truly federal securities no longer existed. Scrooge (and many Englishmen with him) had failed to understand the structure of American government and public finance and had confused Pennsylvania and other state bonds with federal obligations. Just as the introduction of the Euro in 1999 led investors to believe that the shared currency made the debts of Europe’s peripheral economies just as safe as German bunds, so English investors a hundred and sixty years earlier had mispriced the various American state debts. There are no Eurobonds (yet), so a modern equivalent to Scrooge’s metaphor would be as if Scrooge had called Greek bonds “a mere European security”—likening junk to what would presumably be (if it existed) a triple-A rated obligation.

State bonds are not “fiat money,” as economists use that term, but they share at least one characteristic with unsecured paper currency: they depend for their legal value on judicial power to enforce them. Would American courts enforce the bonds of the defaulting American states? That was the question English investors asked their lawyers. State courts were an unpromising venue because of the recognized power of states to invoke sovereign immunity and close their own courts to suitors. Ironically, one of the indebted states did allow suits against itself. Mississippi allowed suit, a case was duly brought, and the plaintiffs won.<sup>5</sup> But the judgment went unsatisfied, and one of the

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4. *Id.* at 23. At the time, bills of exchange were “prepared in three sets as the first, second, and third exchange, so that if one was lost, the others would be available, and once one [was] accepted the others [became] worthless.” CHARLES DICKENS, *THE ANNOTATED CHRISTMAS CAROL* 84 (Michael Patrick Hearn ed. 1976). Dickens had alluded to the subject of American repudiation in his travelogue, *AMERICAN NOTES*, published in 1842, and returned to the subject several times in *MARTIN CHUZZLEWIT*, a long novel that was being published in serial form at the same time as the publication of *A CHRISTMAS CAROL*. CHARLES DICKENS, *AMERICAN NOTES* 245–46 (New Oxford Illustrated Dickens 1957) (1842); CHARLES DICKENS, *THE LIFE AND ADVENTURES OF MARTIN CHUZZLEWIT* 374, 531, 537 (New Oxford Illustrated Dickens 1951) (1843–44).

5. *See generally* *State v. Johnson*, 25 Miss. 625 (1853) (holding that under the constitution and laws of Mississippi a bondholder could sue the state and recover the amount of principal

judges was defeated at the next election.<sup>6</sup>

## I. THE ELEVENTH AMENDMENT: THE EARLY YEARS

The availability of federal courts to enforce state bonds depended on the Eleventh Amendment to the U.S. Constitution. Adopted in 1795 to overturn an earlier Supreme Court decision holding that federal courts had jurisdiction over a suit to collect a state debt brought by a citizen of another state,<sup>7</sup> the Amendment was a response to fear that domestic and foreign creditors could invoke federal jurisdiction to enforce state obligations.<sup>8</sup> The Eleventh Amendment neatly eliminated that risk: “The Judicial power of the United States shall not be construed to extend to any suit in law or equity, commenced or prosecuted against one of the United States by Citizens of another State, [and then added for good measure] or by Citizens or Subjects of any Foreign State.”<sup>9</sup> Bond-holding British subjects appeared to be shut out.

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and interest of the bond).

6. REGINALD MCGRANE, *FOREIGN BONDHOLDERS AND AMERICAN STATE DEBTS* 218 (Beard Books 2000). Mississippi was the first state to provide for the popular election of all its judges. LAWRENCE M. FRIEDMAN, *A HISTORY OF AMERICAN LAW* 127 (2d ed. 1986); see MISS. CONST. of 1832, art. IV, § 2 (“The high court of errors and appeals shall consist of three judges, any two of whom shall form a quorum. The legislature shall divide the State into three districts, and the qualified electors of each district shall elect one of the said judges for the term of six years.”).

7. See *Chisholm v. Georgia*, 2 U.S. 419, 425 (1793). As adopted in 1789, the Constitution gives the Supreme Court jurisdiction over “[c]ontroversies . . . between a State and citizens of another State.” U.S. CONST. art. III, § 2, cl. 1. *Chisholm* was heard in the Court’s original jurisdiction. See U.S. CONST. art. III, § 2, cl. 2 (“In all Cases . . . in which a State shall be Party, the Supreme Court shall have original Jurisdiction.”). Officially recognized by presidential proclamation as part of the Constitution on January 8, 1798, the date traditionally given for its adoption, the Eleventh Amendment had in fact received the necessary number of state ratifications by February 7, 1795.

8. See *Cohens v. Virginia*, 19 U.S. (6 Wheat.) 264, 406–07 (1821) (“It is part of our history, that, at the adoption of the constitution, all the States were greatly indebted; and the apprehension that these debts might be prosecuted in the federal Courts, formed a very serious objection to that instrument. Suits were instituted; and the Court maintained its jurisdiction. The alarm was general; and, to quiet the apprehensions that were so extensively entertained, this amendment was proposed in Congress, and adopted by the State legislatures.”); see also *Alden v. Maine*, 527 U.S. 706, 750 (1999) (“It is indisputable that, at the time of the founding, many of the States could have been forced into insolvency but for their immunity from private suits for money damages.”).

9. U.S. CONST. amend. XI. For an argument that the Eleventh Amendment is a judicial decision in the form of a constitutional amendment, see John V. Orth, *The Judicial Amendment*, 37 J. SUP. CT. HIST. (forthcoming 2012).

Viewed through the gimlet eye of a litigator, however, the wording of the Amendment suggested interesting possibilities. Although it closed the federal courthouse door to suits against states by two classes of plaintiffs—citizens of a state other than the defendant state and citizens (or subjects) of foreign states—it did not exhaust the universe of potential suitors. The obvious lacuna in the Amendment was a suit by a citizen of the debtor state. If citizens could use the federal courts to collect from their own state, it would establish a market for the bonds and give foreign bondholders leverage in negotiations with the debtor state.<sup>10</sup> The Supreme Court closed this loophole in a decision that recognized a federal right to state sovereign immunity in such a case<sup>11</sup>—but not until 1890, when another wave of state defaults after the Civil War and another financial panic generated the mushroom growth of Eleventh Amendment jurisprudence.<sup>12</sup>

Another possibility was suit by a foreign state itself (as opposed to its citizens or subjects). In 1844, the year after the publication of Dickens's *A CHRISTMAS CAROL*, the prominent Massachusetts lawyer, Benjamin Curtis (later a U.S. Supreme Court Justice), acting on behalf of Baring Brothers, published an anonymous article in the influential *North American Review* suggesting just such a strategy.<sup>13</sup> Sovereigns have always taken an interest in the security of their citizens' foreign investments, sometimes forcibly. Sending the gunboats was out of the question in this case, but sending the lawyers might have been possible. This suggestion too was acted upon—but

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10. *Cf. Seminole Tribe v. Florida*, 517 U.S. 44, 122 n.17 (Souter, J., dissenting) (“[N]othing in the treaty [of Paris, 1783] would have prevented foreign creditors from selling their debt instruments (thereby assigning their claims) to citizens of the debtor State.”). The Assignee Clause of the Federal Judiciary Act of 1789 excluded from the diversity jurisdiction of lower federal courts “any suit to recover the contents of any promissory note or other chose in action in favour of an assignee, unless a suit might have been prosecuted in such courts to recover the said contents if no assignment had been made.” Federal Judiciary Act of 1789, ch. 20, § 11, 1 Stat. 73, 79. After the Civil War, the Supreme Court held that the clause was not applicable to securities like bearer bonds that pass by delivery, not assignment. *See, e.g., Thomson v. Lee County*, 70 U.S. 327 (1866) (holding that if a state court construes its laws and constitution to give the bonds force and vitality, the Supreme Court cannot destroy them by a subsequent and contrary construction).

11. *Hans v. Louisiana*, 134 U.S. 1 (1890).

12. *See ORTH, supra* note 1, at 58–109 (describing the history of Eleventh Amendment jurisprudence).

13. Benjamin R. Curtis, *Debts of the American States*, 58 N. AM. REV. 109 (1844). Notably, John Marshall had pointed the way in dicta more than twenty years earlier. *Cohens*, 19 U.S. (6 Wheat.) at 406 (explaining that the Eleventh Amendment “does not comprehend controversies . . . between a State and a foreign State”).

not for another hundred years. In 1934, the Principality of Monaco sued Mississippi in the Supreme Court on its defaulted 1830s bonds with no greater success than in the case of the in-state plaintiff.<sup>14</sup>

Yet another possibility was assignment to an American state (as opposed to its citizens) for collection.<sup>15</sup> This was tried—also many years later—but met with only mixed success.<sup>16</sup> The one surefire winner would have been suit by the United States government.<sup>17</sup> Whether efforts were made in this direction in the 1840s is unknown. There might have been reason to hope: the reputational damage to American credit by the state defaults affected even the federal fisc, which was denied the possibility of a foreign loan in 1842. “Not a dollar,” said Baron Rothschild to the Treasury’s agent.<sup>18</sup> Political constraints imposed by sectionalism probably made federal action infeasible.<sup>19</sup>

It was also possible to approach the problem from the other end, so to speak. Rather than trying to find the right plaintiff, why not try a different defendant? Rather than sue the state itself, why not sue a state officer—say, the state auditor—to compel payment? The Supreme Court under Chief Justice John Marshall had allowed just such a strategy in a suit by the Bank of the United States to recover an unconstitutional state tax collected on one of its branches.<sup>20</sup> “[I]n all cases where jurisdiction depends on the party,” said the Chief Justice, “it is the party named in the record.”<sup>21</sup> A state officer is not a

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14. *Monaco v. Mississippi*, 292 U.S. 313 (1934).

15. Again, John Marshall had signposted the way. See *Cohens*, 19 U.S. (6 Wheat.) at 406 (explaining that the Eleventh Amendment “does not comprehend controversies between two or more States”).

16. See *South Dakota v. North Carolina*, 192 U.S. 286 (1904) (asserting jurisdiction and distinguishing *New Hampshire v. Louisiana* on the ground that New Hampshire had bare legal title, while South Dakota was asserting its own beneficial ownership); *New Hampshire v. Louisiana*, 108 U.S. 76 (1883) (denying jurisdiction); see also *Virginia v. West Virginia*, 206 U.S. 290 (1907) (asserting jurisdiction over the dispute concerning the two states’ liabilities for their respective portions of the antebellum Virginia state debt).

17. See, e.g., *United States v. Texas*, 143 U.S. 621 (1892) (involving a suit by the United States to determine the boundary between U.S. land and land belonging to Texas); *United States v. North Carolina*, 136 U.S. 211 (1890) (involving a suit by the United States against North Carolina to recover interest on bonds issued by the state).

18. Letter from Duff Green to John C. Calhoun (Jan. 24, 1842), reprinted in 2 AM. HIST. ASS’N REP. 841, 842 (1899); see also REPORT OF THE COMMISSIONER SENT TO EUROPE TO NEGOTIATE A LOAN, H.R. DOC. NO. 27-197 (3d Sess. 1843).

19. For a discussion, see Michael S. Greve, *Our Federalism is Not Europe’s. It’s Becoming Argentina’s.*, 7 DUKE J. CONST. LAW & PUB. POL’Y 17 (2012).

20. *Osborn v. Bank of U.S.*, 22 U.S. 738 (1824).

21. *Id.* at 857.

state. A suit against a state officer is, therefore, not a suit against a state. *Q.E.D.* Years later, bondholders tried this route around the Eleventh Amendment, at first with promising results. But finally this, too, turned out to be a dead end.<sup>22</sup>

However many of these legal strategies the state creditors considered in the 1840s, the one thing they did not consider was to sue the debtor states in federal court. Accordingly, the exact bearing of the Eleventh Amendment on American state debt was left undetermined for decades. In fact, also left open was the question to what extent state debts were properly sovereign debts at all (assuming, that is, that a defining characteristic of sovereign debts is their uncollectibility by ordinary legal means).<sup>23</sup> In the 1840s, the creditors' legal situation was not unpromising. Chief Justice Marshall, as we have seen, showed no enthusiasm for the Eleventh Amendment, and Chief Justice Roger Taney never had to take a position on the Amendment during his long tenure.<sup>24</sup> Despite their many differences, both men were firm believers in the reach of federal jurisdiction. Of course, there are many reasons aggrieved parties decide not to litigate other than doubts about jurisdiction: the cost in time and money relative to the likelihood of recovery, their lawyers' skill (or lack thereof) in devising plausible legal arguments, and the chance for an acceptable settlement. In the case of the creditors of the states in the 1840s, the reason seems to have been the prospect of settlements. Many of the antebellum state debts were at least partially redeemed.<sup>25</sup>

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22. Compare *Davis v. Gray*, 83 U.S. 203, 220 (1873) (allowing suit against a state governor, holding that “[w]here the State is concerned, the State should be made a party, if it could be done. That it cannot be done is a sufficient reason for the omission to do it, and the court may proceed to decree against the officers of the State in all respects as if the State were a party to the record.”), and *Bd. of Liquidation v. McComb*, 92 U.S. 531 (1876) (allowing suit against a state board), with *Louisiana ex rel. Elliott v. Jumel*, 107 U.S. 711 (1883) (denying jurisdiction over suit against a state auditor), and *North Carolina v. Temple*, 134 U.S. 22 (1890) (denying jurisdiction over suit against a state auditor).

23. See William B. English, *Understanding the Costs of Sovereign Default: American State Debts in the 1840's*, 86 AM. ECON. REV. 259, 259 (1996) (“These debts are properly seen as sovereign debts both because the United States Constitution precludes suits against states to enforce the payment of debts, and because most of the state debts were held by residents of other states and other countries (primarily Britain.)”); see also THE FEDERALIST NO. 81, at 464 (Alexander Hamilton) (Forgotten Books 2008) (“The contracts between a nation and an individual are only binding on the conscience of the sovereign, and have no pretensions to a compulsive force. They confer no right of action, independent of the sovereign will.”).

24. See ORTH, *supra* note 1, at 42 (“The Amendment was cited in only five cases [during Taney’s tenure as Chief Justice] and in none did the Court find itself ousted of jurisdiction.”).

25. See English, *supra* note 23, at 265 (outlining debts and outcomes in table 3).

## II. STATE DEBT IN THE LATE NINETEENTH CENTURY

When the next wave of American sovereign defaults hit the capital markets in the 1880s, the disappointed bondholders launched a vigorous campaign of litigation, perhaps because the prospect of settlement seemed remote under the circumstances.<sup>26</sup> The result was scant recovery and a remarkable extension of Eleventh Amendment immunity, important parts of which survived the later *revanche* of federal power—indeed, survive to this day.<sup>27</sup> By 1890, precedents had accumulated barring suits to collect state debts brought against state officers, against states by other states, and against states by their own citizens.<sup>28</sup>

The political realities of post-Reconstruction America are more important than legal analysis in making sense of this sudden efflorescence of Eleventh Amendment jurisprudence. To paraphrase Justice Oliver Wendell Holmes, experience rather than logic was the life of the Eleventh Amendment.<sup>29</sup> It is the common coin of American constitutional history that Supreme Court Justices in the late-nineteenth century were unsurpassed in their zeal for freedom of contract and the protection of property.<sup>30</sup> Repudiation must have stunk in their nostrils.

The cases in which the Court stretched the Eleventh Amendment to prevent suits against states all involved suits against states of the Old Confederacy, principally Louisiana and North Carolina.<sup>31</sup> By the time the litigation commenced, Reconstruction was over, the South had recovered “home rule” (that is, rule by the indigenous white male population), and the U.S. Army had been sent back to barracks. Just as the President and Congress abandoned the newly freed slaves after

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26. ORTH, *supra* note 1, at 53–55, 59–60, 63–66, and 90–92 (describing litigation in the 1880s).

27. See discussion *infra* notes 58–68 and accompanying text.

28. The rejection of suits by foreign sovereigns had to wait several more decades.

29. Cf. OLIVER W. HOLMES, JR., *THE COMMON LAW* 5 (1881) (“The life of the law has not been logic; it has been experience.”).

30. See generally ARNOLD M. PAUL, *CONSERVATIVE CRISIS AND THE RULE OF LAW: ATTITUDES OF BAR & BENCH, 1887–1895* (1960) (providing an historical account of legal doctrines used by courts to preserve particular property rights and contractual obligations).

31. Lest there be any confusion, I should make clear that the repudiated bonds in question were issued by the Confederate States of America or by its constituent states. The Fourteenth Amendment made “any debt or obligation incurred in aid of insurrection or rebellion against the United States” illegal and void. U.S. CONST. amend. XIV, § 4. Instead, the bondholders were trying to enforce bonds authorized by Reconstruction legislatures. See, e.g., *Hans v. Louisiana*, 134 U.S. 1, 9 (1890). Or, in some cases, by antebellum legislatures. See, e.g., *North Carolina v. Temple*, 134 U.S. 22 (1890).

Reconstruction, so perforce the former slaves were abandoned by the federal courts.<sup>32</sup> Investors in Southern bonds were abandoned too—and for the same reason. As the attorney general of Louisiana candidly pointed out to the Supreme Court in 1890:

The solemn obligation of a government arising on its own acknowledged bond would not be enhanced by a judgment rendered on such bond. If it either could not or would not make provision for paying the bond, it is probable that it could not or would not make provision for satisfying the judgment.<sup>33</sup>

Without the backing of the political branches, in other words, the courts could not expect their judgments to be satisfied.

The difficulty with that simple solution was that Virginia—arguably the most important state of the Old Confederacy—was denied the shelter of the Eleventh Amendment. A study of the cases shows that the difference resulted from a unique provision included in the covenants of the Virginia bonds, rather than any inherent difference in Virginia’s sovereign immunity: the coupons representing the periodic interest payments were made “receivable at and after maturity for all taxes, debts, dues, and demands due the state.”<sup>34</sup> Again, Chief Justice Marshall provided the clue. In an early case raising an Eleventh Amendment claim, Chief Justice Marshall asked: “Were a State to lay [an unconstitutional] duty on exports,<sup>35</sup> to collect the money and place it in her treasury, could the citizen who paid it . . . maintain a suit in this Court against such a State, to recover back the money?”<sup>36</sup> Answering his question with a dubious “[p]erhaps not,” he continued:

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32. See *The Civil Rights Cases*, 109 U.S. 3, 26 (1883) (holding unconstitutional major portions of the Civil Rights Act of 1875).

33. Brief on behalf of the State of Louisiana at 25, *Hans v. Louisiana*, 134 U.S. 1 (1890) (quoting Letter from Daniel Webster to Baring Bros. & Co. (Oct. 16, 1839), reprinted in *THE PAPERS OF DANIEL WEBSTER: CORRESPONDENCE, VOL. 4: 1835–1839*, at 407 (Charles M. Wiltse & Howard D. Moser eds., 1980)). For a brief discussion of Webster’s rather confusing opinion letter, see ORTH, *supra* note 1, at 43–44. It is one thing for a lawyer to advise a client that a judgment debtor might refuse to pay; it is something else for a debtor’s advocate to tell a court, as a reason not to issue a judgment in favor of the creditor, that such debtor might refuse to pay.

34. Act of March 30, 1871, ch. 282, § 2, 1870–1871 Va. Acts 378, 379.

35. See U.S. CONST., art. I, § 10, cl. 2 (“No State shall, without the Consent of the Congress, lay any Imposts or Duties on Imports or Exports, except what may be absolutely necessary for executing its inspection Laws: and the net Produce of all Duties and Imposts, laid by any State on Imports or Exports, shall be for the Use of the Treasury of the United States; and all such Laws shall be subject to the Revision and Control of the Congress.”).

36. *Cohens v. Virginia*, 19 U.S. (6 Wheat.) 264, 402 (1821).



Suppose a citizen to refuse to pay this export duty, and a suit to be instituted for the purpose of compelling him to pay it. He pleads the constitution of the United States in bar of the action, notwithstanding which the [trial] Court gives judgment against him. This would be a case arising under the constitution<sup>37</sup>

—in other words, a justiciable case.<sup>38</sup>

As applied to the Virginia coupons, this suggested a different legal strategy. Rather than sue the state (or its officers) to compel payment, a bondholder could tender matured coupons in satisfaction of state taxes. To avoid its “solemn obligation,” the state would then have to sue the taxpayer for taxes due and unpaid. Such a suit was quite obviously not a suit against a state, and a judicial decision that the taxes had been legally discharged would not require the court to order the state to make “any provision for satisfying the judgment.” Tender of payment by a debtor at a reasonable time and place and in a reasonable manner is sufficient to satisfy a debt or obligation, whether or not the creditor accepts the payment. In this case, the trial court’s judgment would be self-executing. Taxes are paid when a court of competent jurisdiction says they are. *Ipse dixit*. This strategy was tried and, after much litigation, finally succeeded.<sup>39</sup>

There was also another class of government debt that was not exempted from federal jurisdiction. In the Midwest and West, cities and counties had issued bonds or pledged their credit to encourage railroad construction. In the same year that the Southern states (except Virginia) got their quittance, the Supreme Court held that municipal corporations were not alter egos of the state and were therefore denied the shelter of the Eleventh Amendment.<sup>40</sup> Quoting Chief Justice Marshall, the Court smugly announced: “[T]he eleventh

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37. *Id.* at 402–03. Marshall had posed the same hypothetical case almost twenty years earlier in *Marbury v. Madison*, 5 U.S. (1 Cranch) 137, 179 (1803). See also *Hans*, 134 U.S. at 20–21 (“Whilst a State cannot be compelled by suit to perform its contracts, any attempt on its part to violate property or rights acquired under its contracts, may be judicially resisted, and any law impairing the obligation of contracts under which such property or rights are held is void and powerless to affect their enjoyment.”).

38. *Cohens*, 19 U.S. (6 Wheat.) at 383 (“[A] case arising under the constitution or laws of the United States, is cognizable in the Courts of the Union, whoever may be the parties to that case.”).

39. *E.g.*, *McGahey v. Virginia*, 135 U.S. 662, 664–65 (1890); *In re Ayers*, 123 U.S. 443, 507–08 (1887); *Virginia Coupon Cases*, 114 U.S. 269, 269–70 (1885); *Antoni v. Greenhow*, 107 U.S. 769, 782 (1883); *Hartman v. Greenhow*, 102 U.S. 672, 685 (1881). For the colorful history of Virginia’s determined effort to “readjust” its debt, including statutes commonly known as “coupon killers,” see ORTH, *supra* note 1, 90–105.

40. *Lincoln County v. Luning*, 133 U.S. 529, 530 (1890).

amendment, which restrains the jurisdiction granted by the constitution over suits against states, is of necessity limited to those suits in which the state is a party on the record.”<sup>41</sup> Cities and counties are not states, despite the fact that they derive all their powers—including the power to borrow—from the state. This time, the political branches showed their resolve to back up the courts. Ulysses S. Grant, war hero and President, permitted the publication of a letter stating that he would not hesitate to use force if necessary to see that county debts were honored.<sup>42</sup> In modern terminology, municipal debt is not sovereign; it is subsovereign, which is merely another way of saying that legal means are available to enforce payment. Today, of course, the Federal Bankruptcy Code offers a mechanism for orderly municipal defaults.<sup>43</sup>

### III. EARLY TWENTIETH CENTURY APPROACHES TO SOVEREIGN IMMUNITY

As the problem of Southern state bonds receded into the past, the Supreme Court began the slow process of withdrawing from a few of its more extreme Eleventh Amendment positions. In 1904, a suit by one state against another (and a Southern state at that) to collect on defaulted bonds was allowed.<sup>44</sup> In 1908, the most significant retrenchment occurred. Distinguishing several of the bond cases, the Court held that the Eleventh Amendment did not bar suits against a state officer to prevent violation of the Federal Constitution.<sup>45</sup> Although the Court found that unconstitutional state action was

41. *Id.* (quoting *Osborn v. Bank of U.S.*, 22 U.S. (9 Wheat.) 738, 857 (1824)); *see also* *Bank of U.S. v. Planters' Bank of Ga.*, 22 U.S. (9 Wheat.) 904, 905–06 (1824) (holding that a state-chartered bank is not an alter ego of the state and therefore not eligible to claim Eleventh Amendment immunity). Although cities and counties are in fact organs of state government, they are, in form, chartered corporations. Traditionally, corporations were divided into “municipal corporations” and “corporations other than municipal.” *E.g.*, N.C. CONST. of 1868, arts. VII, VIII; *see* JOHN V. ORTH, *THE NORTH CAROLINA STATE CONSTITUTION*, 140–43 (1993).

42. Letter from Ulysses S. Grant to John A. Dix (June 20, 1870), *reprinted in* CHARLES FAIRMAN, *A HISTORY OF THE SUPREME COURT OF THE UNITED STATES: RECONSTRUCTION AND REUNION 1864–88, PART ONE*, at 985 (Paul A. Freund ed. 1971).

43. *See Ashton v. Cameron Cnty. Water Imp. Dist. No. 1*, 298 U.S. 513, 543 (1936) (“In the public law of the United States a State is a sovereign or at least a quasi-sovereign. Not so, a local governmental unit, although the State may have invested it with governmental power.”).

44. *South Dakota v. North Carolina*, 192 U.S. 286, 313–14 (1904); *see generally* ROBERT F. DURDEN, *RECONSTRUCTION BONDS AND TWENTIETH CENTURY POLITICS: SOUTH DAKOTA V. NORTH CAROLINA* (1904) (1962) (recounting the political and legal controversy surrounding the “South Dakota bond” case).

45. *Ex parte Young*, 209 U.S. 123, 155–56 (1908).

threatened, it nonetheless held that the officer through whom the state acted could not assert the state's sovereign immunity. By attempting to enforce an unconstitutional statute, the state officer is "stripped of his official or representative character and is subjected in his person to the consequences of his individual conduct."<sup>46</sup> As the Supreme Court itself later acknowledged, this holding had the ironical result that a state officer's conduct is state action for purposes of the Fourteenth Amendment but not for purposes of the Eleventh Amendment.<sup>47</sup> Over the course of the twentieth century, that line has wavered but held at the point that exceptions to Eleventh Amendment immunity are permitted insofar as "necessary to permit federal courts to vindicate federal rights and hold state officials responsible to 'the supreme authority of the United States.'"<sup>48</sup>

#### IV. THE ELEVENTH AMENDMENT IN THE LATE TWENTIETH CENTURY

In the last quarter of the twentieth century, the Eleventh Amendment again emerged from obscurity as an activist federal government encountered state concern about liability, and Supreme Court Justices representing different political tendencies disagreed (often forcefully) about the extent of state sovereign immunity.<sup>49</sup> At one time it appeared that the legacy of the Southern bond cases would be limited to preventing judgments against state officers that required drawing money from the state treasury.<sup>50</sup> But this possibility was negated in 1996 by the categorical holding in *Seminole Tribe of Florida v. Florida*:<sup>51</sup> "[T]he relief sought by a plaintiff suing a State is irrelevant to the question whether the suit is barred by the Eleventh Amendment."<sup>52</sup>

*Seminole Tribe* involved what Justice John Paul Stevens aptly called the "rather curious" provision in the Indian Gaming

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46. *Id.* at 160.

47. *Pennhurst State Sch. & Hosp. v. Halderman*, 465 U.S. 89, 105 (1984).

48. *Id.* (quoting *Ex Parte Young*, 209 U.S. at 160).

49. *See Papasan v. Allain*, 478 U.S. 265, 292 (1986) (Brennan, J., dissenting) (describing Eleventh Amendment jurisprudence as a "hodgepodge" of "ad hoc and unmanageable rules bearing little or no relation to one another or to any coherent framework"); *Halderman*, 465 U.S. at 127 (Stevens, J., dissenting) (describing the majority's application of Eleventh Amendment as "perverse").

50. *Papasan*, 478 U.S. at 276-77; *Edelman v. Jordan*, 415 U.S. 651, 663 (1974).

51. 517 U.S. 44 (1996).

52. *Id.* at 58.

Regulatory Act. First, the provision required states to negotiate in good faith with Indian tribes over the regulation of gambling on their reservations. Second, the provision authorized the tribes to sue the states in federal court if they did not.<sup>53</sup> The legal issue was whether Congress could authorize such suits. The majority, in an opinion by Chief Justice William Rehnquist, held that it could not: “The Eleventh Amendment prohibits Congress from making the State of Florida capable of being sued in federal court.”<sup>54</sup> For authority the Court relied on one of the Southern bond cases from 1890, *Hans v. Louisiana*.<sup>55</sup> In *Hans*, an in-state plaintiff had sued his own state—the same case in which the state attorney general had warned the Court concerning the difficulty of enforcing a judgment against the state.<sup>56</sup> The Court in *Hans* found as a historical fact that the adoption of the Eleventh Amendment evidenced an original understanding, broader than the literal terms of the Amendment, that states were not subject to suit in federal court without their consent.<sup>57</sup> It therefore dismissed the suit for want of jurisdiction.<sup>58</sup> In *Seminole Tribe*, the plaintiff tribe had also joined the state’s governor as a defendant, but the majority rejected this claim, too, inferring that Congress did not contemplate jurisdiction over a state officer because the legislation prescribed “a

53. *Id.* at 77 (Stevens, J., dissenting).

54. *Id.* at 76. Despite this sweeping statement, the Chief Justice elsewhere in his opinion recognized that Congress did have the power to make a state susceptible to suit in federal court if acting pursuant to its enforcement power under the Fourteenth Amendment. *Id.* at 59 (citing *Fitzpatrick v. Bitzer*, 427 U.S. 445, 455 (1976)).

55. 134 U.S. 1 (1890).

56. *See Hans*, 134 U.S. at 9 (“The question is presented, whether a State can be sued in a Circuit Court of the United States by one of its own citizens upon a suggestion that the case is one that arises under the Constitution or laws of the United States.”).

57. *See id.* at 15 (“Can we suppose that, when the eleventh amendment was adopted, it was understood to be left open for citizens of a state to sue their own state in the federal courts, while the idea of suits by citizens of other states, or of foreign states, was indignantly repelled? . . . The supposition that it would is almost an absurdity on its face.”).

58. I have not discussed the issue of state consent to suit in this paper, although it is germane to the general issue of federal jurisdiction over states. Despite holding that the Eleventh Amendment and the associated concept of state sovereign immunity deprive federal courts of jurisdiction over suits against states, the Supreme Court has consistently held that federal courts may exercise jurisdiction over suits against states that consent. *See, e.g., Coll. Sav. Bank v. Fla. Prepaid Postsecondary Educ. Expense Bd.*, 527 U.S. 666, 670 (1999) (“[A] State may waive its sovereign immunity by consenting to suit.”). State consent to suit is the unique instance in which a party may confer jurisdiction on the Court. *See Seminole Tribe v. Florida*, 517 U.S. 44, 127–28 (1996) (Souter, J., dissenting) (“[C]onsent of a party is in all other instances wholly insufficient to create subject-matter jurisdiction where it would not otherwise exist.”). Since the question here is whether state debts are sovereign, I have limited my remarks to cases in which consent to suit is denied.

detailed remedial scheme” in case a state refused to comply.<sup>59</sup>

Justice David Souter, writing on behalf of three other Justices, filed a long dissenting opinion, extensively reviewing the historical literature.<sup>60</sup> Turning the history lesson against the majority, Justice Souter wrote that “*Hans* is so utterly indefensible on the merits of its legal analysis that one is forced to look elsewhere in order to understand how the Court could have gone so far wrong.”<sup>61</sup> “[H]istory,” he said, “provides the explanation,”<sup>62</sup> and pointed to “the pattern of the cases, which tends to show that the presence or absence of enforcement difficulties significantly influenced the path of the law in this area.”<sup>63</sup> Thus, Justice Souter would have limited *Hans* to cases brought under the constitutional grant of jurisdiction over suits involving states and citizens of another state (so-called “citizen-state diversity jurisdiction”).<sup>64</sup> For cases against a state arising under the Constitution (“federal question jurisdiction”),<sup>65</sup> state sovereign immunity would exist as only a matter of federal common law, waivable by congressional legislation.

Seemingly irked, Chief Justice Rehnquist responded that the dissent “disregards our case law in favor of a theory cobbled together from law review articles and its own version of historical events” and concluded that “[i]ts undocumented and highly speculative extralegal explanation of the decision in *Hans* is a disservice to the Court’s traditional method of adjudication.”<sup>66</sup> While the Chief Justice may

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59. *Seminole Tribe*, 517 U.S. at 74 (majority opinion). Under the Indian Gaming Regulatory Act, the remedy for failure by a state to negotiate in good faith is an order directing the state and the tribe to conclude a compact within sixty days. The remedy for failure to comply with this order is an order that each party submit a proposed compact to a mediator who selects the one that best embodies the terms of the statute. Finally, the remedy for failure by a state to accept the compact selected by the mediator is notice to the Secretary of the Interior who then implements regulations governing gambling on the tribal lands. Indian Gaming Regulatory Act, 25 U.S.C.A. § 2710 (West 2012).

60. The historical literature included (I must admit) my book and later law review article. See ORTH, *supra* note 1 (tracing the history of Eleventh Amendment jurisprudence); John V. Orth, *The Truth About Justice Iredell’s Dissent in Chisholm v. Georgia*, 73 N.C. L. REV. 255 (1994) (discussing misunderstanding and misrepresentation of Justice Iredell’s dissent).

61. *Seminole Tribe*, 517 U.S. at 122 n.17 (Souter, J., dissenting).

62. *Id.* at 120; see also *id.* at 122 (“[H]istory explains, but does not honor, *Hans*.”).

63. *Id.* at 121 n.16.

64. See U.S. CONST. art. III, § 2 (“The judicial Power shall extend . . . to Controversies . . . between a State and Citizens of another State . . .”).

65. See *id.* (“The judicial Power shall extend to all Cases, in Law and Equity, arising under this Constitution, the Laws of the United States, and Treaties made, or which shall be made, under their Authority . . .”).

66. *Seminole Tribe*, 517 U.S. at 68–69; see also *Coll. Sav. Bank v. Fla. Prepaid*

have a point about the explanation being “extralegal,” in the sense that it is not based on what appears in the U.S. Reports (and perhaps about its “speculative” nature, based as it is on “the pattern of the cases”), he overstates his point about the forensic use of history. The Court in *Hans*—like the Court in many other constitutional cases—purported to base its decision on “its own version of historical events.”<sup>67</sup> As Justice Souter justly observed in reply, “[t]his Court’s opinions frequently make assertions of historical fact,” although he qualified this observation with the recognition that “these assertions are not authoritative as to history in the same way that our interpretations of laws are authoritative as to them.”<sup>68</sup>

Although the majority readily acknowledged the historical context of the adoption of the Eleventh Amendment, it refused to consider the historical context of the decision in *Hans*. Perhaps this is what the Chief Justice meant by “the Court’s traditional method of adjudication.” Although it is characteristic of forensic legal history to treat historical facts as relevant to the understanding of legal documents such as statutes or constitutions (or constitutional amendments), judges tend to treat judicial decisions as ahistorical, perhaps because to emphasize the particular historical context of a decision would detract from the appearance of judicial impartiality.

Supreme Court cases are not adjudications of historical fact. (In this country we are fortunately spared an official history.) Whether or not the Court in *Hans* found its version of the past merely a convenient explanation for dismissing a case it could not handle for other reasons, the decision it rendered was an interpretation of the Eleventh Amendment—or, rather of Article III of the Constitution, in light of the Eleventh Amendment. The dissenters in *Seminole Tribe* thought *Hans* was wrong as a matter of constitutional construction. It is certainly plausible to argue that they found historical arguments convenient as a way to marginalize a decision with which they

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Postsecondary Educ. Expense Bd., 527 U.S. 666, 688 (1999) (referring to “the now-fashionable revisionist accounts of the Eleventh Amendment set forth in other opinions in a degree of repetitive detail that has spoiled our northern woods”).

67. *Seminole Tribe*, 517 U.S. at 68–69.

68. *Id.* at 108 n.5 (Souter, J., dissenting). It is also worth noting the riposte by Chief Justice Appleton of Maine to Chief Justice Taney’s use of history in *Dred Scott v. Sanford*, 60 U.S. 393 (1856): “[W]hatever may be the authoritative force of a decision of the Supreme Court of the United States, there can be no doubt that its statements, as to the past history of the country, are binding neither on the historian nor the jurist.” *Burton v. Kennebec*, 44 Me. 405, 561 (1857).

disagreed. But it is also plausible to argue that the majority in *Seminole Tribe* defended *Hans* not only as a matter of historical accuracy and stare decisis but also because it suited their preference for restricting the reach of federal power over the states. If the expansive Eleventh Amendment decisions in the Southern state bond cases were driven by fears of nonenforcement, that fear was surely absent in *Seminole Tribe*. The federal court could safely have ordered Florida to negotiate with the tribe “in good faith” (for whatever good that would do).

## V. MODERN CONSEQUENCES

Because sovereign debts have come to be defined by their legal enforceability—or, rather, lack thereof—whether American state debts are “sovereign” depends on whether the creditors can secure an enforceable judgment in federal court. The U.S. Constitution does not by its terms generally preclude “suits against states”—quite the contrary. Instead, state suability depends (as we have seen) on exactly who is suing the state. The Eleventh Amendment and its associated doctrines bar the usual plaintiffs seeking to collect state debts: private investors both domestic and foreign. To that extent, American state debts are sovereign. But the Eleventh Amendment and associated doctrines do not bar all suits against states,<sup>69</sup> not even all suits to collect state debts. Other American states have sued debtor states in federal court and won (and collected).<sup>70</sup> And it has never been doubted that the federal government itself could sue states in federal court.<sup>71</sup> Although states are immune from suit by most plaintiffs, state officers are not, if necessary to prevent violations of federal constitutional rights.<sup>72</sup> But the sovereign immunity of states (such as it is) does not extend to their political subdivisions.<sup>73</sup> Here the question is whether the governmental entity is more like a state or a county, a question that has proved difficult to answer with respect to some of

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69. See *Nevada v. Hall*, 440 U.S. 410, 420 n.19 (1979) (“[T]he Eleventh Amendment has not accorded the States absolute sovereign immunity in federal-court actions.”).

70. *South Dakota v. North Carolina*, 192 U.S. 286 (1904).

71. *United States v. Texas*, 143 U.S. 621 (1892); *United States v. North Carolina*, 136 U.S. 211 (1890); see also *Seminole Tribe*, 517 U.S. at 71 n.14 (reaffirming *United States v. Texas*).

72. See, e.g., *Ex parte Young*, 209 U.S. 123 (1908); see also *Seminole Tribe*, 517 U.S. at 71 n.14 (reaffirming *Ex parte Young*).

73. See, e.g., *Lincoln County v. Luning*, 133 U.S. 529 (1890); see also *N. Ins. Co. of N.Y. v. Chatham County*, 547 U.S. 189, 193 (2006) (“[T]his Court has repeatedly refused to extend sovereign immunity to counties.”).

the modern commissions and authorities that states have created.<sup>74</sup>

The scars of the struggle over the enforceability of state debts remain visible today, not only on the jurisdiction of federal courts, but also on the creditworthiness of Southern states. In North Carolina, for example, the state constitution adopted in 1971 carries forward a provision that the General Assembly “shall never . . . assume or pay any . . . bond . . . issued” between 1868 and 1870 unless payment is approved “by a majority of all of the qualified voters at a referendum held for that sole purpose.”<sup>75</sup> Lest this embarrassment impair the state’s current credit rating, the same constitution gives investors in later issues extraordinary protection. Although the governor has the duty to maintain a balanced budget by “making necessary economies in State expenditures,” that duty is subject to the significant proviso that she must first make “adequate provision for the prompt payment of the principal of and interest on bonds and notes of the State according to their terms.”<sup>76</sup> Modern bondholders, in other words, are first in line in case of a revenue shortfall, ahead of school children and the indigent—probably a necessary proviso in light of the state’s credit history, but one that the unreformed Ebenezer Scrooge would doubtless have applauded.

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74. *See, e.g.*, *Cash v. Granville Cnty. Bd. of Educ.*, 242 F.3d 219 (4th Cir. 2001) (holding that a principal factor in determining the sovereign status of a governmental entity is whether a judgment against the governmental entity would have to be paid from the state’s treasury).

75. N.C. CONST. art. V, § 3 (4). The original version of this provision dates to a post-Reconstruction amendment added to the state’s 1868 constitution in 1880 and carried over into the state’s 1971 constitution. *See ORTH, supra* note 41, at 123–24.

76. N.C. CONST. art. III, § 5 (3). This provision, requiring a balanced budget, was added to the state’s 1971 constitution by amendment in 1977. *ORTH, supra* note 41, at 94–96. Lest this addition raise doubts about the inviolability of subsequently issued state debt, the provision expressly preserves the obligation of bonds or notes “issued hereafter.” N.C. CONST. art. III, § 5 (3). The North Carolina Supreme Court has held that taxpayers have standing to challenge a governor’s actions under this subsection. *Goldston v. State*, 637 S.E.2d 876 (N.C. 2006). In a later stage of the same case, the extent of the governor’s power to reallocate appropriated funds was clarified by the North Carolina Court of Appeals, a decision affirmed by an equally divided state supreme court. *Goldston v. State*, 683 S.E.2d 237 (N.C. Ct. App. 2009), *aff’d*, 700 S.E.2d 223 (N.C. 2010) (affirming the lower-court decision by a divided supreme court and without precedential value).