CORE
Metadata, citation and similar papers at core.ac.uk
Provided by Penn Law: Legal Scholarship Repository

University of Pennsylvania Carey Law School
Penn Law: Legal Scholarship Repository

Faculty Scholarship at Penn Law

2018

Foreword: Bankruptcy's New and Old Frontiers

William W. Bratton
University of Pennsylvania Carey Law School

David A. Skeel Jr.
University of Pennsylvania Carey Law School

Follow this and additional works at: https://scholarship.law.upenn.edu/faculty_scholarship

Part of the Bankruptcy Law Commons, Business Organizations Law Commons, Corporate Finance Commons, Law and Economics Commons, Legal History Commons, and the Securities Law Commons

Repository Citation
Bratton, William W. and Skeel, David A. Jr., "Foreword: Bankruptcy's New and Old Frontiers" (2018). *Faculty Scholarship at Penn Law*. 2026.
https://scholarship.law.upenn.edu/faculty_scholarship/2026

This Article is brought to you for free and open access by Penn Law: Legal Scholarship Repository. It has been accepted for inclusion in Faculty Scholarship at Penn Law by an authorized administrator of Penn Law: Legal Scholarship Repository. For more information, please contact PennlawIR@law.upenn.edu.

UNIVERSITY *of* PENNSYLVANIA
LAW REVIEW

Founded 1852

Formerly
AMERICAN LAW REGISTER

© *2018 University of Pennsylvania Law Review*

VOL. 166 | JUNE 2018 | NO. 7

FOREWORD

BANKRUPTCY'S NEW AND OLD FRONTIERS

WILLIAM W. BRATTON† & DAVID A. SKEEL, JR.‡

I. THE BIRTH OF CORPORATE REORGANIZATION........................1573
II. REIMAGINING BANKRUPTCY IN THE NEW DEAL...................... 1576
III. CORPORATE REORGANIZATION UNDER THE 1978 CODE 1579
IV. MAKING SENSE OF THE NEW FRONTIERS 1584
A. *The New Bond Workouts*.. 1584
B. *The Bankruptcy Partition* 1585
C. *Corporate Bankruptcy Hybridity.* 1587
D. *Taking Control Rights Seriously* 1588
E. *Bankruptcy's Uneasy Shift to a Contract Paradigm* 1589

† Nicholas F. Gallicchio Professor of Law and Co-Director, Institute for Law & Economics, University of Pennsylvania Law School.
‡ S. Samuel Arsht Professor of Corporate Law, University of Pennsylvania Law School.

F. *Valuation Disputes in Corporate Bankruptcy* 1589
G. *The Creditors' Bargain Revisited* 1590
V. THE WAY FORWARD? 1592

This Symposium marks the fortieth anniversary of the enactment of the 1978 Bankruptcy Code (the "1978 Code" or the "Code") with an extended look at seismic changes that currently are reshaping Chapter 11 reorganization. Today's typical Chapter 11 case looks radically different than did the typical case in the Code's early years. In those days, Chapter 11 afforded debtors a cozy haven. Most everything that mattered occurred within the context of the formal proceeding, where the debtor enjoyed agenda control, a leisurely timetable, and judicial solicitude. The safe haven steadily disappeared over time, displaced by a range of countervailing forces and a cooperative bankruptcy bench. Lenders, especially debtor-in-possession (DIP) financers,[1] gradually began to shape the trajectory of many proceedings. They today determine the course of most of the cases. More recently, additional players such as hedge funds and equity funds have also entered the scene, altering the bargaining dynamic. New financial instruments complicate debtors' capital structures and creditor incentives. Even the sites and modes of decisionmaking have shifted, as today's key decisions are negotiated and embedded in contracts concluded even before the debtor files for bankruptcy. The changes, which continue to accumulate, are fundamental.

Congress has given a gentle assist to a few of these changes.[2] Sometimes this has followed from direct intervention, as when Congress amended the Code to diminish the debtor's agenda control of judicial reorganization proceedings.[3] At other times the effect is indirect, as when Congress encouraged the use of derivatives and other new financial instruments by largely exempting them from key bankruptcy provisions such as the automatic stay that requires other creditors to halt any collection efforts.[4] Whether direct or indirect, most of the legislative interventions have been of minor importance and the statutory framework is largely identical to that enacted in 1978. The changes have been driven by innovations in reorganization practice and judicial interpretation. It is a dynamic situation.

1 The Bankruptcy Code provides for new funding for a debtor that has filed for bankruptcy in section 364. 11 U.S.C. § 364 (2012). When a debtor files for bankruptcy, it becomes the "debtor-in-possession." *See* 11 U.S.C. §§ 1101(1), 1107 (2012). The new financing is known as debtor-in-possession or "DIP" financing.

2 Congress has made numerous amendments to the 1978 Code, including substantial reforms in 1994 and 2005. But it has not passed a complete overhaul.

3 The Code gives the debtor the exclusive right to present a plan for the first 120 days of the proceeding. Formerly, some courts would indefinitely extend the exclusivity right. Since 2005, the Code cuts off the extensions after 18 months. *See* 11 U.S.C. §1121(d)(2)(A) (2012).

4 11 U.S.C. § 561 (2012).

Some of the most important and controversial of these new developments, such as the use of restructuring support agreements to lock up votes for a potential reorganization, will likely have seen further evolution by the time this Foreword appears in print.

This Foreword provides context for the Symposium's academic contributions by recounting the historical developments that have brought us where we are. After chronicling the origins, New Deal redirection, and recent evolution of corporate reorganization, we describe some of the remarkable and often counterintuitive insights the articles in this Symposium offer for the current moment. We conclude by venturing a few thoughts about the future. As we shall see, the Nietzschean vision of history as eternal recurrence has surprising explanatory power in the bankruptcy context.[5]

I. THE BIRTH OF CORPORATE REORGANIZATION

American corporate reorganization first emerged in the late nineteenth century, facilitated by a dramatic common law innovation, the federal equity receivership. The new procedure was first applied to what were then the country's only publicly held corporations, the railroads, and was later extended to other corporations.[6]

The railroads filled a vital need, providing timely and affordable transportation for food, manufactured goods, and people. But the growth and expansion of the private railway companies was haphazard. Entrepreneurs competing to control essential routes, such as New York to Chicago, raced to build track and acquire smaller railroads, waging epic battles over key links such as the Erie Railway.[7] During flush periods, the railroads attracted huge amounts of capital and investment, most of it debt capital. When the economy crashed, as it did with some regularity during the nineteenth century, numerous railroads defaulted.

The default of a substantial railroad posed a serious dilemma. Since the railroads were crucial to America's future, there was an enormous public

5 As Friedrich Nietzche proclaimed, "[w]hat if a demon crept after you into your loneliest loneliness some day or night, and said to you: 'This life, as you live it at present, and have lived it, you must live it once more, and also innumerable times; and there will be nothing new in it, but every pain and every joy and every thought and every sigh, and all the unspeakably small and great in your life must come to you again, and all in the same series and sequence and similarly this spider and this moonlight among the trees, and similarly this moment, and I myself. The eternal sand glass of existence will ever be turned once more, and you with it, you speck of dust!'" FRIEDRICH NIETZSCHE, THE GAY SCIENCE § 341 (Walter Kaufman trans., Random House 1974) (1887).

6 Many of the developments in this part are described in greater detail in DAVID A. SKEEL, JR., DEBT'S DOMINION: A HISTORY OF BANKRUPTCY LAW IN AMERICA 48-70 (2001).

7 *See generally* JOHN STEELE GORDON, THE SCARLET WOMAN OF WALL STREET: JAY GOULD, JIM FISK, CORNELIUS VANDERBILT, THE ERIE RAILWAY WARS, & THE BIRTH OF WALL STREET (1988).

interest in rescuing and sustaining them. A defaulting line's creditors were likely to see things the same way, favoring reorganization over liquidation. Despite this pervasive support, the most obvious strategies for facilitating a reorganization faced serious constitutional obstacles.[8] Today, there are no doubts about Congress's ability to pass a reorganization law. In the nineteenth century, by contrast, the Commerce Clause was much more narrowly construed, and might not have provided constitutional authority for a reorganization law. Congress's other source of authority, the Bankruptcy Clause, was similarly shaky, because there were serious questions regarding whether a reorganization law would impermissibly encroach on the chartering state's role as the principal regulator of corporations. In theory, a railroad's state of incorporation could pass a railroad reorganization law. Unfortunately, such a state-level enactment would have amounted to an idle gesture, for states could not alter existing contracts and had no power to regulate beyond their borders—a potentially crippling limitation given a multi-state railroad.

It was against this backdrop that the equity receivership emerged. When a railroad defaulted, its creditors would commence two related actions, often in coordination with the line's managers: first, bondholders who held mortgages on some of the assets would ask the court to commence a foreclosure proceeding; second, other creditors would ask the court to turn control over all of the company's assets to a receiver. The bondholder plaintiffs in the first action, rather than asking for a prompt foreclosure sale, would ask the court to put the sale on hold. During the intervening weeks, the investment banks that had sold the railroad's stock and bonds would form committees to represent each different type of security. The debtor and the committees would negotiate the terms of a restructuring. Once terms had been agreed upon, the parties would combine the committees into one large reorganization committee. The bondholder plaintiffs would then ask the court to schedule the foreclosure sale. The only bidder at the sale would be the reorganization committee, which would submit a bid consisting of the bonds and stock held by the investors who had agreed to be represented by a committee, together with enough cash to pay dissenting investors.[9]

The process the parties concocted was the world's first large scale corporate reorganization framework, an invention borne of necessity. But the equity receivership did not emerge fully formed like Athena from Zeus's

8 SKEEL, *supra* note 6, at 52–56 (describing various constitutional considerations).

9 In the words of Paul Cravath, namesake of the Cravath firm and the leading reorganization lawyer of his time, "Counsel who have acted frequently for reorganization committees have spent a great many anxious hours preparing for the unexpected bidder, but in my own experience he has never appeared." Paul D. Cravath, *Reorganization of Corporations: Certain Developments of the Last Decade*, *in* 1 SOME LEGAL PHASES OF CORPORATE FINANCING, REORGANIZATION, AND REGULATION 204 (Francis Lynde Stetson et al. eds., 1917).

head. The parties confronted a variety of obstacles, which they solved through contract, court approval, or both. Because most railroads were fully encumbered with mortgages when the receivership commenced, it might be impossible for them to borrow the funds they needed to continue operating during the receivership, since the new money would be subordinate to the existing mortgage liens. The reorganizers solved this problem by creating "receiver's certificates." If the court approved a receiver's certificate, it was given the first share of the debtor's revenues, before they ever got to the mortgage bondholders. Receiver's certificates were the forerunner to what we now call DIP financing.[10]

Another problem was the cost of paying dissenting bondholders and stockholders—the investors who refused to "deposit" their securities with the committees. Paying these investors in full would have invited holdouts and undermined the composition process, since investors who declined to deposit their securities would get paid much more than those who participated in the restructuring. To solve this problem, the reorganizers persuaded courts to set an "upset price." This price was ostensibly the fair value of the defaulted security. Rather than paying dissenters in full, the reorganization committee, as winning bidder, was only required to pay them the upset price. This significantly diminished the incentive to hold out, especially when the reorganizers persuaded the court to set a low upset price.[11]

There was also a question regarding the priority status of unsecured creditors vis-à-vis shareholders, a question that famously came to the fore in an early twentieth century case, *Northern Pacific Railroad v. Boyd*.[12] There, a creditor who had been wiped out in a reorganization that gave a continued stake to the railroad's old shareholders, despite the shareholders' lower priority, challenged the receivership as fraudulent.[13] The Supreme Court vindicated the creditor, holding that the exclusion from participation was impermissible.[14] This was a serious complication, because shareholder support was thought to be essential to the receivership process, in part because shareholders often contributed new funds to the reorganization. Reorganizers once again created a clever workaround: they started inviting

10 Relatedly, courts developed the doctrine of necessity to address the need to pay suppliers. This is the forerunner to what we now call critical vendor doctrine. *See, e.g.*, *In re* Kmart Corp., 359 F.3d 866, 871 (2004) (discussing the origins of the doctrine of necessity).

11 *See* Joseph L. Weiner, *Conflicting Functions of the Upset Price in a Corporate Reorganization*, 27 COLUM. L. REV. 132, 142 (1927) (considering upset price from the point of view of the reorganization committee). The upset price also was used to compensate third parties whose claims were released.

12 228 U.S. 482 (1913).

13 *Id.* at 488.

14 *Id.* at 510.

general creditors to participate in the receivership, but only if they too agreed to pay a cash subscription toward the effort.[15]

The question of the parties' respective priority rights also prompted the most important scholarly exchange of the equity receivership era. In a 1927 article, the leading corporate reorganization lawyer of the time argued that mortgage holders' priorities should not be strictly enforced, because reorganizers needed flexibility to craft a reorganization plan.[16] The following year, two other legal scholars identified this as the "relative priority" approach and contrasted it with "absolute" priority, posing two "rival" priority schemes.[17] They criticized the malleability of the relative priority approach, but concluded that some version of it was probably inevitable.[18] It turned out that relative priority was not quite as inevitable as they thought, at least in the short run. A decade later it would be gone.

II. REIMAGINING BANKRUPTCY IN THE NEW DEAL

The Depression brought stresses and strains to the corporate reorganization system, leading to two congressional interventions. The first, in 1933 and 1934, straightened out some dysfunctional elements in equity receivership practice but otherwise did little to disrupt the process. Dissatisfaction with the inherited system grew as the decade wore on, resulting in a second, completely transformative intervention in 1938.

The equity receivership mechanism ceased to function reliably in the wake of the economy's collapse. The upset price emerged as a barrier because reorganizing companies lacked the cash to pay even a low-ball sum. The New Dealers came to the rescue with the Bankruptcy Acts of 1933 and 1934, which codified large-scale corporate reorganization for the first time.[19] The initial legislation removed barriers from the existing playing field but otherwise did little to disrupt the process context.

The leading reorganizers warmly embraced the 1934 legislation, lobbying actively in support. An essential contribution of the new provisions, as they saw it, was a new voting rule, which facilitated the approval of a plan of reorganization by a majority of the creditors and overrode bond contract

---

15 *See, e.g.*, ROBERT T. SWAINE, 1 THE CRAVATH FIRM AND ITS PREDECESSORS: 1819–1906 497 (1946) (highlighting the use of the Boyd decree strategy).

16 Robert T. Swaine, *Reorganization of Corporations: Certain Developments of the Last Decade*, 27 COLUM. L. REV. 901, 907 (1927).

17 *See* James C. Bonbright & Milton M. Bergerman, *Two Rival Theories of Priority Rights of Security Holders in a Corporate Reorganization*, 28 COLUM. L. REV. 127, 130 (1928) (differentiating between the theory of relative priority and the theory of absolute priority).

18 *Id.* at 165.

19 *See* Act of June 7, 1934, ch. 424, § 77B, 48 Stat. 911 (repealed 1938) (summarizing reorganization protocol for non-railroads).

provisions requiring unanimous consent to amendments of terms.[20] This gave the committees the power to bind dissenters to the plan and removed the need to pay them a cash upset price. Codification also removed concerns that courts might restrict the use of the receivership process outside of the railroad context.

The next phase of reform was less congenial to the reorganization establishment. In the mid-1930s, the newly formed Securities and Exchange Commission conducted a massive study of large-scale reorganization cases. Led by William O. Douglas, then a law professor at Yale, the SEC investigators interviewed well over one hundred participants in the major recent receivership cases, which they chronicled in a multivolume report.[21] Douglas and his colleagues—including Abe Fortas, who, like Douglas himself, later became a Supreme Court Justice—found evidence of fraud and other misbehavior, and concluded that ordinary investors were poorly served by the Wall Street banks and lawyers who dominated the committee-driven receivership process. In a speech before the Eastern Law Students Conference in Washington D.C., Douglas accused his fellow lawyers of having forgotten their vow as lawyers to put their clients' interests before their own. "[T]here has been a degeneration of the bar in these situations," he complained.[22] "Conflicts of interest have had their corroding influence."[23]

The concerns of those behind the SEC study and of scholars sympathetic to their mission can be distilled to three major objectives. First, they believed that reorganization should be much more closely monitored by the courts. Under existing practice, courts did not come into the picture until the end of the process, after the parties had worked out the details and were ready for the "sale" to take place under the equity receivership or the plan to be confirmed under the 1934 legislation. The reformers called for judicial oversight from the proceeding's beginning. The second objective concerned technical wherewithal. Judicial oversight, by itself, would not suffice. Administrative expertise also was needed in the service of investor protection because appropriate outcomes in a complex reorganization required a wider range of neutral, expert input than followed from neutral adjudication of a litigated issue.[24] The third objective was "democracy." Under current practice,

---

20 *See* Robert T. Swaine, *An Open Letter Containing Proposals for Amendment of the Bankruptcy Act So As to Aid in Combating the Depression*, *in* Symposium, *Corporate Reorganization Under the Federal Bankruptcy Power*, 19 VA. L. REV. 317, 333-34 (1933) (setting forth the "essentials" of a measure to address "the appalling extent of financial and industrial distress").

21 SECURITIES AND EXCHANGE COMMISSION, REPORT ON THE STUDY AND INVESTIGATION OF THE WORK, ACTIVITIES, PERSONNEL AND FUNCTIONS OF PROTECTIVE AND REORGANIZATION COMMITTEES (1937).

22 WILLIAM O. DOUGLAS, DEMOCRACY AND FINANCE: THE ADDRESSES AND PUBLIC STATEMENTS OF WILLIAM O. DOUGLAS 233 (James Allen ed., 1940).

23 *Id.*

24 *Id.* at 194-95.

investors had no real say in the process once they had deposited their bonds with a committee. The reformers believed that the process needed to be democratized, and that investors should be the ones to determine the outcome, either directly or through representatives they freely elect.[25]

During this same period, Congressman Chandler of Tennessee had introduced an extensive set of bankruptcy reforms, many of which were technical adjustments to the provisions that applied in consumer and small business cases. In 1937, Douglas, who had become the SEC's chairman, persuaded advocates of the Chandler bill to include in the legislation a new, SEC-drafted chapter applicable to large corporations. The new chapter, Chapter X, was enacted in 1938. It sharply increased the judicial and administrative role by requiring that the debtor's managers be replaced by a court-appointed trustee, by providing for judicial oversight throughout the case, and by requiring that the SEC be given an opportunity to scrutinize most proposed reorganization plans and deliver an evaluation directly to the confirming court. Although Chapter X did not eliminate committee representation altogether, it did provide for a direct vote on the plan by investors—not the committee—thus enhancing the democracy of the process.[26]

One risk was that the reorganizers would attempt to evade the new framework by restructuring large corporations outside of bankruptcy. The reformers anticipated this possibility, and sought to preempt it the following year. The Trust Indenture Act of 1939 (TIA) included a provision—the creditor consent requirement of section 316(b)—that prohibits a corporation from imposing a modification of a bond's payment terms on a particular bondholder absent the bondholder's consent. This provision made it illegal to apply majoritarian voting provisions (known today as "collective action clauses" or "CACs") to the payment terms in corporate bonds. It followed that judicially supervised bankruptcy reorganization, now built around majority-approved plans to which dissenters were bound, provided the only viable venue in which to effect a bond workout.

The same year, Douglas, whose meteoric rise had by then landed him on the Supreme Court, held that the ambiguous term "fair and equitable" in the Bankruptcy Act of 1934 required strict adherence to the absolute priority

25 The reformers generally emphasized the first option—a meaningful vote by investors on the plan—but at least one reformer advocated representative democracy. *See* Roger S. Foster, *Book Review*, 43 YALE L.J. 352, 357 (1933) (reviewing MAX LOWENTHAL, THE INVESTOR PAYS (1933)). For a scathing critique of the democratization effort by the leading reorganization lawyer, see Robert T. Swaine, *"Democratization" of Corporate Reorganizations*, 38 COLUM. L. REV. 256 (1938).

26 *See* Mark Roe characterizes the advent of New Deal oversight as the first of three "ages" of American bankruptcy law in a recent article. Mark J. Roe, *Three Ages of Bankruptcy*, 7 HARV. BUS. L. REV. 187, 188 (2017) (describing the "rise and dominance of administration, deal, and sale [which] make for three ages of bankruptcy."). As the text reflects, we parse the history slightly differently, identifying equity receivership as the opening gambit and finding recurring themes in the periods that follow.

rule,[27] even though none of the Supreme Court's absolute priority cases had ever actually adopted the usage relied upon.[28] The adoption, which carried over to Chapter X under the Chandler Act of 1938, amounted to a give back to dissenters. If, under majoritarian voting, a creditor could be forced to accept reduced principal or interest payments or other impairment of its claim, it was thought to be unfair simultaneously to permit any junior claimant to participate in the reorganization. It followed that old shareholders would not be permitted to retain a stake in the reorganized company even if higher priority creditors voted to approve it. This increased the safeguards for ordinary investors, most of whom held bonds in this era, even as it narrowed the range of their "democratic" options.

The interpolation of absolute priority also built in additional dependence on outside technical expertise. Under the absolute priority rule, a senior class of creditors must be paid "in full" in some form before any junior claimant could receive a participation under the reorganization plan. Given payment in the form of a new security issued by the reorganized company (and in the absence of a trading market in the reorganized firm's securities), it takes a full-dress valuation of the reorganized company to support a judicial ruling that the new security being issued to the creditor class in fact amounts to payment "in full." Thus would the SEC scrutineers in Chapter X focus closely not just on the plan's terms, but also on the supporting valuation of the corporate debtor.[29]

The old receivership practice withered away after the Chandler Act of 1938 was enacted, very much as the reformers intended. Their court-centered framework held sway for the next forty years.[30]

III. CORPORATE REORGANIZATION UNDER THE 1978 CODE

The new Code enacted in 1978 greatly relaxed the restrictions that the New Deal reformers had put in place for large corporate reorganizations. Chapter 11, the new reorganization chapter, not only permitted managers to continue running the business, rather than replacing them with a court-appointed trustee; it also gave managers the exclusive right to propose a reorganization plan for at least the first four months of the case.[31] The Code also gave the parties more flexibility with respect to the terms of a possible

27 *See* Case v. L.A. Lumber Prods. Co., 308 U.S. 106, 121-22 (1939).

28 John D. Ayer, *Rethinking Absolute Priority after* Ahlers, 87 MICH L. REV. 963, 975 (1989) ("Strictly speaking, this is poppycock, and Justice Douglas knew it.").

29 For the classic, critical account of valuation in this era, see Walter J. Blum & Stanley A. Kaplan, *The Absolute Priority Doctrine in Corporate Reorganizations*, 41 U. CHI. L. REV. 651 (1974). *See also* Walter J. Blum, *The Law and Language of Corporate Reorganization*, 17 U. CHI. L. REV. 565 (1950).

30 For discussion of the erosion of the New Deal framework that took place after the first decade of the Chandler Act, see SKEEL, *supra* note 6, at 161-68.

31 11 U.S.C. §§ 1107, 1121(b) (2012).

reorganization plan. Rather than applying the absolute priority rule to every class of claimant and every reorganization plan, the rule could be invoked only on the contingency that a given class of claimants rejected the proposed plan and then only would be applied as to the complaining class.[32] If a sufficient majority of a class voted to approve the plan,[33] the absolute priority rule could be waived. Overall, these changes reduced the need for judicial oversight and shifted authority back to the negotiating parties themselves—a shift augmented by the elimination of the SEC's role as advisor and watchdog. At the same time, the decision to allow creditors to waive the absolute priority rule expanded the range of creditor democracy in bankruptcy.[34]

Wall Street reorganization practice reemerged after forty years in the wilderness under the 1978 Code, rejuvenated by Chapter 11's new framework. Since corporate managers no longer faced immediate displacement by a trustee, they were more willing to file for bankruptcy. For some firms, bankruptcy even became a plausible strategic option, rather than an absolute last resort.[35] Within a few years, nearly every major law firm had started (and begun touting) a bankruptcy practice.[36]

The Code era of the past four decades has not followed a single trajectory—it has included at least two, and possibly three, phases. In the first phase, which lasted a little over a decade, the managers of a debtor enjoyed significant agenda control after filing for bankruptcy. Because courts routinely extended their four-month "exclusivity period," sometimes for years, managers could weaken creditors' resistance by implicitly threatening to drag the case out indefinitely. There were complaints that managers used their leverage to extract deviations from absolute priority from the creditors, although the deviations were never as pronounced as the complaints sometimes implied.[37]

The second phase began in the mid-1990s and reached maturity after 2000. In this phase creditors effectively used contractual provisions to

---

32 Under 11 U.S.C. § 1129(b), the absolute priority rule only applies "with respect to each class of claims or interests that is impaired under, and has not accepted, the plan."

33 For a class of creditors, two-thirds by amount and more than one-half of the number of claimants; for an equity class, two-thirds in amount. *See* 11 U.S.C. §§ 1126(c), (d) (2012).

34 The drafters did not show the same confidence in the voting process in consumer bankruptcy cases. Under the old law, creditors voted whether to approve a payment plan approved by a consumer debtor. Chapter 13, which now governs proposed payment plans, does not provide for a creditor vote.

35 *See generally* KEVIN J. DELANEY, STRATEGIC BANKRUPTCY: HOW CORPORATIONS AND CREDITORS USE CHAPTER 11 BANKRUPTCY TO THEIR ADVANTAGE (1998).

36 *See, e.g.,* Leonard M. Rosen & Jane Lee Vris, *A History of the Bankruptcy Bar in the Second Circuit*, *in* THE DEVELOPMENT OF BANKRUPTCY & REORGANIZATION LAW IN THE COURTS OF THE SECOND CIRCUIT OF THE UNITED STATES 155, 156 (1995) (noting that forty-nine of the top fifty New York law firms claimed to have a bankruptcy practice).

37 *See* Lynn M. LoPucki & William C. Whitford, *Bargaining Over Equity's Share in the Bankruptcy Reorganization of Large, Publicly Held Companies*, 139 U. PA. L. REV. 125, 126 (1990) (describing the deviations as a "tempest in a teapot").

counteract the debtor-friendly features of the 1978 Code. Debtor-in-possession financers sometimes insisted on the appointment of a chief restructuring officer before or shortly after a debtor's bankruptcy filing.[38] They also included covenants in their loan agreements that restricted the debtor's discretion to manage the proceeding. For example, in the FAO Schwartz case (2003), the DIP loan included a covenant that required the debtor to liquidate if it failed to propose a confirmable reorganization plan by a specified date.[39] The provision had the effect of eliminating management's ability to use the threat of delay to extract concessions from creditors. The lenders in the United Airlines bankruptcy (2002) used tight cash flow constraints—a requirement that the debtor generate a specified amount of cash in excess of expenses—to force the company to renegotiate its collective bargaining agreements with employees.[40]

Proceedings also became quicker during the second phase. Under the new practice, increasing numbers of debtors could largely avoid the cumbersome process of a traditional reorganization either by selling all of their assets or by seeking judicial approval of a fast-track, prepackaged bankruptcy. The sale route often is taken at the insistence of a DIP lender which agrees to finance the debtor's Chapter 11 case only if the debtor commits to conduct a sale within thirty or sixty days of filing. In a prepackaged bankruptcy (a strategy used several times by President Trump in the 1990s), the debtor negotiates an out-of-court workout of its principal debt—usually bonded debt—and then encases the negotiated workout in a reorganization plan filed simultaneously with its bankruptcy petition. The objective is to enter and exit bankruptcy within two or three months.

These developments altered bankruptcy practice so significantly that a leading bankruptcy lawyer wrote an article lamenting the beleaguered Chapter 11 debtor.[41] The trends have continued. They have not as yet fully displaced more traditional Chapter 11 reorganizations. But displacement at times has seemed likely.

We appear to have entered a third, current phase. The features of creditor control vis-à-vis the debtor continue to dominate the landscape. But the cast

---

38 *See* Douglas G. Baird & Robert K. Rasmussen, *The End of Bankruptcy*, 55 STAN. L. REV. 751, 784-785 (2002) (describing the implicit power of the lender in a DIP financing arrangement).

39 *See* David A. Skeel, Jr., *Creditors' Ball: The New "New" Corporate Governance in Chapter 11*, 152 U. PA. L. REV. 917, 926 n.34 (2003) (describing DIP financing agreement in FAO Schwartz bankruptcy).

40 *See id.* (detailing United Airlines' attempt to "extract deep concessions from its unions" as a result of cash flow targets set by the lender).

41 Harvey R. Miller & Shai Y. Waisman, *The Creditor in Possession: Creditor Control of Chapter 11 Reorganization Cases*, 21 BANKR. STRATEGIST 1 (2003). Tellingly, Harvey Miller temporarily left his law firm and joined an investment bank (Greenhill) before returning to his law firm partnership. Another leading bankruptcy lawyer, Jamie Sprayregen, followed the same track, going to Goldman Sachs and then returning.

of characters has lengthened, with hedge funds and other distressed debt professionals joining DIP lenders as major players. New financial contracts also are having an impact. Credit derivatives are redirecting lender incentives in uncooperative directions.[42] But other modes of contracting promote cooperation. In a first and second lien lending arrangement, the second lienholders usually agree to defer to the first lienholders on key issues, and sometimes even to vote as instructed by the first lienholders in a later bankruptcy.[43] Restructuring support agreements are used by distressed debtors and their lenders to secure advance support for a Chapter 11 reorganization plan. In some cases, the later, formal vote on the proposed plan is largely a formality, because large majorities of most classes of creditors have already committed to vote in favor by contract.[44]

Troubled corporations also have devised clever strategies for reorganizing outside of bankruptcy. Although the TIA forbids direct amendment of bond payment terms without an individual bondholder's consent, distressed firms have long used exchange offers paired with coercive "exit consents" to encourage large bondholder majorities to agree to a restructuring effected by exchange rather than direct amendment. This strategy has seen a dramatic increase in use and effectiveness in the past several years.[45]

As we look at the current moment through the lens of bankruptcy history, it is not hard to see patterns of recurrence and chiasm.[46] Recent bankruptcy practice has remarkable similarities to the old equity receivership era of the late nineteenth and early twentieth centuries. Now, as then, the parties manage the process through contractual agreements they negotiate among themselves. Although the agreements theoretically are subject to judicial oversight once the debtor files in Chapter 11, there often is little the court realistically can do to upset them. This is most evident when the DIP financer insists on a prompt sale of the debtor's assets. Although a bankruptcy judge theoretically could reject the timeline proposed in the DIP loan, the lender often can credibly threaten to withhold funding and let the debtor collapse unless the court approves the terms. Bankruptcy judges have a more meaningful opportunity to scrutinize restructuring support agreements. But

---

42 *See, e.g.*, Douglas G. Baird & Robert K. Rasmussen, *Antibankruptcy*, 119 YALE L.J. 648, 680-86 (2010) (describing how credit default swaps influence bankruptcy negotiations).

43 *See* Kenneth Ayotte, Anthony J. Casey, & David A. Skeel, Jr., *Bankruptcy on the Side*, NW. U.L. REV. 255, 260 (2017) (discussing potential benefits stemming from side agreements, as well as the dangers).

44 Douglas G. Baird, *Bankruptcy's Quiet Revolution*, 91 AM. BANKR. L.J. 593, 605 (2017) (discussing the legality of such non-binding informal agreements).

45 This development is explored in detail in William W. Bratton, Jr. & Adam J. Levitin, *The New Bond Workouts*, 166 U. PA. L. REV. 1597 (2018).

46 A chiasma takes the form A-B-B'-A', where the initial theme (A), gives way to a second theme (B), the second theme is developed (B'), then the initial theme returns, in a way that harkens back to the beginning but also somehow alters or transforms it.

here too the path of least resistance is to approve the agreement, much as most courts did in the equity receivership era.

In the current phase, the question whether absolute or relative priority is preferable has once again assumed critical importance. In its most important recent bankruptcy case, the Supreme Court invalidated an increasingly common circumvention of absolute priority—a practice called structured dismissal—much as it did a century ago in the *Boyd* case.[47] This decision came in the wake of controversies over several other recent practices that stand in tension with the absolute priority rule, and of a passionate debate in the legal literature featuring many of the participants of this Symposium.[48]

A few unusual bankruptcy cases have drawn even more directly from the receivership era, resurrecting the receivership process itself. In the bankruptcies of Chrysler and General Motors, the parties conducted a "sale" that transferred the debtors' assets to a newly formed entity consisting largely of the debtor's old creditors, just as used to happen in railroad receiverships.[49] The managers of the largest financial institutions, now required to prepare annual "living wills," signal that they plan to use essentially the same process in the event of financial distress.[50]

As in the receivership era, nearly all of these developments have been driven by innovations in practice and judicial decisions, rather than legislative change. There are, of course, massive differences between the current era and the old equity receiverships. Unlike the early twentieth century, when markets were poorly developed, there is much more liquidity now. This makes it possible to find actual, third party buyers for the assets even of large firms. But many of the issues are remarkably similar.

47 Czyzewski v. Jevic Holding Corp., 137 S. Ct. 973, 983 (2017) (holding that a bankruptcy court cannot "approve a structured dismissal that provides for distributions that do not follow ordinary priority rules without the affected creditors' consent"). For a thoughtful analysis of *Jevic*, see Bruce Grohsgal, *Absolute Priority Redux: First-Day Orders and Pre-Plan Settlements in Chapter 11 Post-*Jevic, 10 WM. & MARY BUS. L. REV. (forthcoming 2018).

48 For recent critiques of absolute priority, see Douglas G. Baird, *Priority Matters: Absolute Priority, Relative Priority, and the Costs of Bankruptcy*, 165 U. PA. L. REV. 785, 821 (2017); Anthony J. Casey, *The Creditors' Bargain and Option-Preservation in Chapter 11*, 78 U. CHI. L. REV. 759, 711 (2011). For a defense, see Barry E. Adler & George G. Triantis, *Debt Priority and Options in Bankruptcy: A Policy Intervention*, 91 AM. BANKR. L.J. 563, 579-81 (2017).

49 *See, e.g.,* Stephen J. Lubben, *No Big Deal: The GM and Chrysler Cases in Context*, 83 AM. BANKR. L.J. 531, 544 (2009) (summarizing the similarity between Chrysler and railroad receiverships); Mark J. Roe & David A. Skeel, Jr., *Assessing the Chrysler Bankruptcy,* 108 MICH. L. REV. 727, 732 (2010) (noting that "the Chrysler reorganization handled a practical business problem via a sale format as did the equity receivership's reconstruction of the American railroad system").

50 Under this strategy—known as the "single point of entry" approach—the holding company of the troubled financial institution will transfer its assets and some of its debt to a newly created entity. *See* Randall D. Guynn, *Framing the TBTF Problem: The Path to a Solution* (describing implementation of the single point of entry strategy), *in* ACROSS THE GREAT DIVIDE: NEW PERSPECTIVES ON THE FINANCIAL CRISIS 281, 295 (Martin Neal Baily & John B. Taylor eds., 2014).

IV. MAKING SENSE OF THE NEW FRONTIERS

The current era has seen both radical innovation in the financial markets and a return of some of the issues and strategies that characterized restructuring practice a century ago. The participants in this Symposium thus are seeking to make sense of an unusual and at times disorienting moment.[51]

A. *The New Bond Workouts*

The long hand of history can influence contemporary debt restructuring in unexpected ways. One such moment of influence was an unexpected turn in the case law treated in William Bratton and Adam Levitin's *The New Bond Workouts.* In a cluster of cases decided in 2014 and 2015, courts in the Southern District of New York, the nation's leading forum for bond litigation, adopted a novel and broad reading of the creditor consent provision in TIA section 316(b).[52] The new reading made bond workouts harder to close and was greeted with much consternation in the practice world. The status quo was, however, later restored when the Second Circuit reversed the leading Southern District case in an opinion steeped in Depression-era legislative history.[53]

Bratton and Levitin use the occasion of this case law flare up to take a new look at workout practice and reconsider a longstanding policy question concerning the repeal of section 316(b). Their projection of a world without section 316(b) follows the pattern of historical recurrence, making reference to a forgotten body of cases dating from the equity receivership era.

Bratton and Levitin draw on an original dataset to report on a remarkable transformation in workout practice. In the received picture, bond workouts are dysfunctional and tend to fail to close. Bondholders hold out and free ride in response to restructuring offers from distressed debtors. Debtors respond in kind, utilizing a variety of coercive inducements and procedural maneuvers. The result is a destabilizing and potentially toxic mix of creditor opportunism and debtor coercion that tends to derail the collective decisionmaking process. The Depression-era legislative inheritance doubles down on the dysfunction by taking the possibility of direct amendment of bond contract payment terms off the table in TIA section 316(b), a provision

51 As were Judge Marjorie Rendell in her opening keynote on the first day critiquing the expansion of equitable mootness doctrine, and, on day two, Professor Troy McKenzie in his analysis of the starkly different implications of legislative silence in bankruptcy as compared to administrative law.

52 *See* BOKF, N.A. v. Caesars Entm't Corp., 144 F. Supp. 3d 459, 467 (S.D.N.Y. 2015) ("[S]ection 316(b) protects a noteholder's practical ability, as well as the legal right, to receive payment when due"); Meehancombs Glob. Credit Opportunities Funds, LP v. Caesars Entm't Corp., 80 F. Supp. 3d 507, 518 (S.D.N.Y. 2015) (same); Marblegate Asset Mgmt. v. Educ. Mgmt. Corp., 75 F. Supp. 3d 592, 613 (S.D.N.Y. 2014) (same), *rev'd*, 846 F.3d 1 (2d Cir. 2017).

53 Marblegate Asset Mgmt., LLC v. Educ. Mgmt. Fin. Corp., 846 F.3d 1 (2d Cir. 2017).

that largely accomplished its purpose of making federal bankruptcy the exclusive (and more costly) venue for corporate debt restructuring. Bratton and Levitin show that the situation has changed. Workouts are now working, albeit with coercive tactics figuring more prominently than ever in the recent fact patterns. The markets have learned how to live with section 316(b), denuding the longstanding policy case for its removal of much of its urgency.

At the same time, Bratton and Levitin show that section 316(b) no longer accomplishes much in the way of bondholder protection and that there no longer is any reason to fear that out-of-court restructuring by majority amendment will systematically disadvantage bondholders. They recommend repeal accordingly, with the post-repeal process and voting rules left over to the determination of the drafters of bond contracts. But the authors also enter a caveat, based on their analysis of a second original dataset that tracks changes in the drafting pattern of Rule 144A bonds in the wake of the Southern District's adoption of the broad reading of section 316(b). They predict that drafting in the wake of repeal will be responsive to bondholder concerns without also producing a complete set of protective process instructions. Abuses that beg for judicial policing could follow. Unfortunately, today's judges lack the tools to do the job. Precisely because section 316(b) succeeded in channeling restructuring into the well-policed precincts of bankruptcy, the federal equity doctrine that policed out-of-court restructuring during the equity receivership era—the doctrine of intercreditor good faith duties—atrophied after 1945. The authors recommend its resuscitation, commending it for providing a more fact-sensitive and targeted tool for policing overreaching in bond workouts than the Southern District's broad reading of section 316(b).

B. *The Bankruptcy Partition*

The old dispute between absolute and relative priority recently reared its head once again at the United States Supreme Court in *Czyzewski v. Jevic Holding Corp*.[54] The Court, as it has consistently done for a century, adhered to absolute priority, with negative implications for a number of practices in contemporary bankruptcy proceedings. The particular question for decision was highly technical and concerned a bankruptcy court's power to order a "structured" dismissal; that is, a dismissal of a Chapter 11 petition that determines the rights of a party or parties rather than just returning all parties to their prepetition situations.[55] The structured dismissal at issue in *Jevic* distributed the proceeds of a settlement of a claim held by the bankruptcy

54 137 S. Ct. 973 (2017).
55 *Id.* at 979-80.

estate to the company's general creditors, skipping over a class of priority wage claimants.[56] The dismissal's proponent argued that the priority violation was justified on the facts of the case because it maximized overall returns to the creditors.[57] Furthermore, it had statutory backing under a provision of the Bankruptcy Code which permitted the court to "order otherwise" in connection with a dismissal, "for cause."[58] The Supreme Court found the backing inadequate, refusing to carve out a "rare case" exception—rare though the case may have been, there was no justification for bypassing the statute's bedrock substantive precept.[59]

In *The Bankruptcy Partition*, Douglas Baird, Anthony Casey and Randall Picker offer a new approach for working through the issue not only in *Jevic*, but in a large collection of cases that routinely arise in today's Chapter 11 proceedings. The article builds on three core insights, all derived from the creditors' bargain theory. First comes a maximand: claimants focus on the maximization of the value of the enterprise in which they invest, rather than on the maximization of their aggregate wealth as a group of individuals. Second, the terms of the creditors' bargain follow from the maximand—the creditors' bargain pertains only to the enterprise's bankruptcy estate, which is in turn partitioned off from the various interests of individual creditors. Third, the purpose of bankruptcy law is to provide a process that maximizes the value of the bankruptcy estate. The article's critical conclusion follows from these insights: in a case like *Jevic* the salient question is not whether a bankruptcy reorganization should follow an absolute or relative priority scheme, but rather whether the subject matter under dispute lies inside or outside the bankruptcy partition. If the subject matter lies inside, its value should be maximized; if the subject matter lies outside, the outcome (maximization or not) is of no concern to the system.

A line drawing exercise follows. A given creditor's claim against the debtor in possession is clearly inside; a dispute between two creditors as regards a third-party debtor clearly lies outside. The paper focuses on difficult cases that lie between the two extremes, drawing the line between inside and outside. That accomplished, the paper looks more closely at the implications of the goal of maximizing the value of the estate. The goal justifies aggressive policing of the conduct of opportunistic claimants by the bankruptcy judge. Estate value maximization also leads to contracting between the estate and

---

56 *Id.* at 980-81.

57 *See In re* Jevic Holding Corp., 787 F.3d 173, 185 (3d Cir. 2015), *rev'd*, 137 S. Ct. 973 (2017) ("[the settlement], unsatisfying as it was, remained the least bad alternative since there was 'no prospect' of a plan being confirmed and conversion to Chapter 7 would have resulted in the secured creditors taking all that remained of the estate in 'short order.'").

58 11 U.S.C. § 349(b) (2012).

59 *Jevic*, 137 S. Ct. at 987.

outsiders—transactions that cross the partition. As to these, the fact that the transaction holds out benefits to a prepetition creditor should not of itself lead to prohibitive intervention on distributive grounds, for contracts normally lead to benefits for both counterparties. At the same time, occasions for judicial policing are likely to arise when a prepetition creditor is also a postpetition contract counterparty.

Baird, Casey, and Picker work within this framework to provide a nuanced template for treatment of a range of recurring issues, among them, third-party releases, senior-to-junior gifting, vote designation, contracts with vendors, roll ups, settlements, and other postpetition transactions between the debtor and prepetition creditors.

C. *Corporate Bankruptcy Hybridity*

Whereas Baird, Casey and Picker seek to chart the boundaries of bankruptcy, distinguishing in and out, Melissa Jacoby trains her attention on a tension within bankruptcy itself in *Corporate Bankruptcy Hybridity*: the relationship between bankruptcy's public and private dimensions. Jacoby begins by repudiating the assumption that corporate bankruptcy should focus "solely on wealth maximization, voluntary lenders, and investors."[60] Jacoby argues that the preoccupation with welfare maximization deflects attention from the public dimension of bankruptcy, and has abetted the increasing privatization of the bankruptcy process. Bankruptcy should be viewed, instead, as a public-private partnership. Jacoby is particularly concerned with bankruptcy's democratic legitimacy. Drawing on a range of studies, she points out that procedural justice is essential to maintaining the legitimacy of legal systems. Her focus on democratic values echoes the concerns of the New Deal reformers, but takes them in a strikingly new direction to consider not just traditional creditors, but the victims of discrimination of a debtor like Bethlehem Steel and others who are affected by a corporate debtor's bankruptcy.

One of the culprits in Jacoby's account is venue selection, which enables many large corporate debtors to file their bankruptcies in New York or Delaware. The cases often are far from ordinary parties' homes, thus making it difficult for them to participate in the case. The equitable mootness doctrine undermines the public function of bankruptcy in a different but related way. By thwarting appeals, equitable mootness reduces the institutional check on deals struck by private parties. Jacoby also criticizes the strong resistance to appointing a trustee in Chapter 11 cases, contending that an independent trustee is more likely than the debtor-in-possession or the creditors' committee to police misbehavior or seek to avoid prebankruptcy

60 Melissa Jacoby, *Corporate Bankruptcy Hybridity*, 166 U. PA. L. REV. 1715, 1716 (2018).

transfers. Lenders may further disarm public oversight by insisting on protection from avoidance actions, as in the much discussed *Jevic* case. Jacoby proposes the creation of a Sunlight Fund "designed to reduce the ability of private parties with leverage to deter estate-enhancing and public-value-promoting activity."[61] Jacoby concludes by decrying the absence of diversity in corporate bankruptcy scholarship, attributing the dearth of attention to public values in part to the homogeneity of the most widely-cited scholars.

D. *Taking Control Rights Seriously*

In *Taking Control Rights Seriously*, Robert Rasmussen revisits an issue he first took up in a classic 2002 article: the control exerted by debtor-in-possession financers.[62] The earlier article was among the first to identify the rise of lender influence, and it treated this development as a central feature of a radically changing bankruptcy landscape in which traditional Chapter 11 reorganizations were being displaced by going concern sales. The 2002 article, like other work that followed it, focused on the lenders' seeming hegemony. In *Taking Control Rights Seriously*, Rasmussen takes the inquiry into creditor control in the opposite direction, asking why lenders do not insist on even greater control. Although it may seem hard to imagine that lenders could assert more influence than they already do, Rasmussen remarks that the Bankruptcy Code leaves existing control rights largely untouched, instead focusing far more on cash flow rights. The strategies that lenders have devised to shape the managers' behavior and the bankruptcy case consist of vetoes and checks rather than true control rights. Tight covenants give lenders the power to limit capital expenditures, for instance, or dictate the timeline of the bankruptcy case. They do not, however, give lenders direct control.

Why, then, do creditors not insist on true control rights, such as the power to remove the chief executive officer or place representatives on the board of directors if the debtor defaults? Says Rasmussen, it is possible that the current strategy is optimal: "The reason for being circumspect in control could be that giving formal control rights to lenders upon certain triggering events would raise the specter of opportunistic behavior."[63] But the absence of lender control rights may also reflect a less benign combination of managers' desire to retain control and lenders' fear that they could face lender liability litigation or equitable subordination if they took a more direct role in the business. The risk of legal constraints thus impedes desirable control arrangements. Rasmussen suggests that companies be given the right to waive

61 *Id.* at 1743.

62 Baird & Rasmussen, *supra* note 38, at 784-85.

63 Robert Rasmussen, *Taking Control Rights Seriously*, 166 U. PA. L. REV. 1749, 1770 (2018).

lender liability and equitable subordination in their corporate charters, a proposal that subtly links the concerns of Rasmussen's early and more recent work.

E. *Bankruptcy's Uneasy Shift to a Contract Paradigm*

Like Rasmussen, David Skeel and George Triantis are concerned with the parties' intentions as reflected in actual contracts, rather than hypothetical ones. In the 1990s, economics-oriented scholars often criticized the mandatory structure of the Bankruptcy Code, and advocated greater freedom to contract over alternatives. Examining the Code and its historical context, Skeel and Triantis contend that bankruptcy law is not nearly as mandatory as common wisdom suggests, especially as compared to the former Bankruptcy Act. The Code invites the parties to contract over key features of bankruptcy, and the parties now seize the opportunity, as many of the authors in the Symposium point out here and in other work.

But there's a catch, Skeel and Triantis argue: the endorsement of contracting is unbalanced. While courts and the Code facilitate ex post contracting, they are much more hostile to ex ante contracts. Drawing on contracting theory, Skeel and Triantis consider the costs and benefits of ex ante and ex post contracting. Although ex post contracts do offer genuine benefits—they take place in an information rich environment, for instance—ex ante contracts, where information is more limited, can promote reliance and allocate monitoring responses.[64] Skeel and Triantis conclude that courts should be less hostile to ex ante contracts such as intercreditor agreements. More counterintuitively, they also contend that courts have been too quick to accommodate ex post contracts. Although courts are understandably reluctant to disrupt agreements that the parties reach ex post, even a unanimously approved agreement may inefficiently unravel the parties' ex ante commitments.

F. *Valuation Disputes in Corporate Bankruptcy*

As we have seen, judicial valuation is a central—indeed unavoidable—component of absolute priority review of a Chapter 11 reorganization plan. It is also a notoriously difficult factual inquiry, a mode of judicial proceeding famous for susceptibility to manipulative inputs from claimants, their counsel, and their hired experts. We have also seen that the drafters of the Chandler Act of 1938 attempted to solve the manipulation problem by mandating SEC input on the valuation question.

64 In their comments on the article, Judge Michelle Harner and Professor Patrick Bolton each emphasized that an additional benefit of ex post contracting is the judicial oversight and transparency provided by bankruptcy.

Valuation lost its central place in Chapter 11 plan confirmation when the Code was redesigned in 1978, making absolute priority review an option contingent on classwide dissent rather than an absolute requirement. Under the conventional wisdom during the first phase of the history of post-1978 Chapter 11 practice, judicial valuations would be the exception rather than the rule under the new system. The parties would resolve doubts in favor of supporting a plan of reorganization to avoid the uncertainty and expense of a valuation proceeding, at least as regarded a big, publicly traded debtor. At the same time, scholars during the 1978 Code's first phase devoted a great deal of energy to devising new approaches to corporate reorganization that would altogether obviate the need to value the debtor in court.

In *Valuation Disputes in Corporate Bankruptcy*, Kenneth Ayotte and Edward Morrison return bankruptcy valuation practice to a front and center position. They study 143 cases entailing a valuation dispute decided since 1990, showing at a minimum that today's parties do not shrink from contesting points of valuation. Around one-third of the cases arose in connection with plan confirmation disputes. The rest are split between valuation issues in connection with avoidance of fraudulent or preferential transfers, adequate protection disputes, claims allowance, dismissals, and section 363 sales.

Professors Ayotte and Morrison catalogue the valuation techniques employed and patterns of disputation, highlighting soft points where lawyers succeed at luring judges away from adherence to financial economic orthodoxy. Even as the background of financial learning has become much more extensive and sophisticated since 1938, it seems that the hoodwinking of judges remains a salient problem. Opinions allowing small "premium" add-ons to discount rates derived pursuant to the capital asset pricing model for use in discounted cash flow valuations come in for particularly sharp criticism. Judicial performance in comparable company and comparable transaction valuation gets higher marks—these inquiries depend more on common sense than on theoretical training and aptitude. Overall, the authors recommend a more "confined and standardized toolkit than the wide-open space that currently exists," making very specific suggestions that get the bankruptcy courts from here to there.

G. *The Creditors' Bargain Revisited*

For the past generation, the creditors' bargain model, which conceptualizes bankruptcy as a hypothetical bargain addressing creditors' collective action problems, has exerted a gravitational pull both on those sympathetic to its logic and on those who reject its premise that bankruptcy has a single objective. In *The Creditors' Bargain Revisited*, Barry Adler returns to one of his best known articles, which offered a novel alternative to current

Chapter 11 for solving creditors' collective action problems.[65] Under Adler's approach, firms would issue "Chameleon Equity" that would convert from debt to equity if the debtor failed to cure a default. The past decade has seen the emergence of financial instruments such as contingent convertible bonds that could be a tentative first step toward the regime Adler envisioned. Here was the opportunity for a little victory lap.

But *The Creditors' Bargain Revisited* pivots in a very different direction. Prompted by suggestions from bankruptcy practitioners that "if freed from legal constraint, creditors would not only contract out of bankruptcy but out of *any* collective proceeding," Adler speculates that the much vaunted collective action problem might not be a problem at all.[66] The "race to the courthouse" could actually be a *solution*—a consummation devoutly to be wished. Shutting down companies that are unable to pay their debts might be more efficient than giving them a bankruptcy option, Adler suggests, or perhaps a debtor's principal creditors could determine whether to preserve the firm even in the absence of bankruptcy. Adler concludes that bankruptcy may not be necessary at all. Its only real contribution, perhaps, is to "launder" the firm's assets by assuring that any sale or discharge is free and clear of existing interests.

***

A RETROSPECTIVE LOOK AT BANKRUPTCY'S NEW FRONTIERS. The creditors' bargain model of bankruptcy looms so large in bankruptcy scholarship that it is easy to forget that the theory was devised by a real person at a particular point in time. The best antidote is of course to hear from the originator himself. And we did. At the conference giving rise to the Symposium, Tom Jackson recounted the origins of the theory in the years immediately after the Bankruptcy Code was enacted. He has turned his address into an essay that reveals the serendipity that often attends the emergence of pathbreaking ideas, and which we predict will occupy a significant place in the annals of American financial history.[67] Jackson, who has returned to bankruptcy scholarship and policy after years as a law school dean and university president, also turns his attention to the current moment, mentioning

65 Barry E. Adler, *Financial and Political Theories of American Corporate Bankruptcy*, 45 STAN. L. REV. 311, 323-24 (1993); *see also* Barry E. Adler, *Bankruptcy and Risk Allocation*, 77 CORNELL L. REV. 439, 445 n.19 (1992) ("A neutral legal environment that permits firms meaningfully to opt out of bankruptcy could prompt virtually all firms to solve the collective action problem with contracts prior to any investor's contribution of capital.").

66 Adler's speculation is foreshadowed by another key article. *See* Barry E. Adler, *A Theory of Corporate Insolvency*, 72 N.Y.U. L. REV. 343, 351 (1997) (arguing that the "collective action problem is largely illusory").

67 *See generally* Thomas H. Jackson, *A Retrospective Look at Bankruptcy's New Frontiers*, 166 U. PA. L. REV. 1867 (2018).

his own important work on bankruptcy for banks and assessing recent developments such as the renewed debate over absolute and relative priority and the increased prevalence of going concern sales in recent Chapter 11 cases.

V. THE WAY FORWARD?

In the views of many, the dramatic market innovations of the past several decades have permanently transformed American corporate reorganization. The best known of these interventions—written by participants in this Symposium—proclaimed the "end of bankruptcy" as new techniques and expanded markets made the traditional reorganization process unnecessary.[68] One of us also has written in this vein.[69]

Two implicit claims inform the case that bankruptcy has moved on from its point of origin to a qualitatively different place. First, contemporary business is so different from that of the nineteenth-century railroads that the traditional model of reorganization has lost its relevance. The railroads had a hierarchical structure and were seen to further a public interest, factors which made them apt candidates for the state-controlled reorganization context. Contemporary firms are far less hierarchical and can easily morph their corporate structure, making it more likely that they can succeed in restructuring on their own.[70] Second, contemporary markets have become so fully developed as to render reorganization largely unnecessary. The value of a nineteenth century railroad could only be realized through a restructuring, because potential buyers did not have access to sufficient capital to purchase the entire firm. In the twenty-first century, by contrast, capital flows so freely that buyers can easily be found for any valuable line of business or valuable firm. There is no longer any going concern value, this line of reasoning concludes, that can only be preserved by a state-sponsored, collective proceeding.

Although the changes in firms and in the markets in which the firms rise and fall are indeed profound, we remain persuaded that the pattern is more of recurrence than of fundamental transformation—or termination. Although market innovation clearly has altered corporate reorganization practice, many of today's pressing questions are remarkably similar to the questions of the past. Critics worry that there is not enough judicial oversight of key transactions such as sales of most or all of the company's assets. There are debates about the compensation of bankruptcy professionals and about whether ordinary creditors are sufficiently protected. William O. Douglas surely would nod his head in recognition if he heard these complaints.

68 Baird & Rasmussen, *supra* note 38, at 785.

69 *See, e.g.,* Skeel, *supra* note 39, at 922 (noting that changes in the profiles of businesses in bankruptcy and contractual developments introduced new incentives to corporate managers).

70 *See* Roe, *supra* note 26, at 214-16 (emphasizing the tendency toward decentralization).

The key recurring theme of American bankruptcy, in our view, is the tension between the terms and effects of consensual arrangements reached by the parties and a perceived need for government intervention to correct potential distortions and third-party effects. Start with the consensual arrangements. In the bankruptcy context, these arrangements are generally contractual, whether they take the form of contracts that parties entered into prior to financial distress, implicate later renegotiation of such contracts, or are new contracts entered into during the financial distress. Sometimes renegotiation takes place prior to bankruptcy—as with the bond exchanges addressed by Bratton and Levitin. Sometimes renegotiation takes place in bankruptcy—as with the structured dismissals discussed by Baird, Casey, and Picker. Sometimes the parties facilitate reorganization by entering new contracts such as restructuring support agreements.

Although deference to consensual arrangements runs deep, so too does the perception that the parties cannot simply be left to their own devices. According to the classic expression of this theme, dating back to the mid-twentieth century, markets cannot be trusted to be self-regulating.[71] In current bankruptcy, judicial oversight of the bankruptcy process is the most pervasive governmental function. The bankruptcy judge oversees nearly every facet of the process, from resolving objections to the parties' claims to confirming a proposed reorganization plan.[72] In addition, the government supplies technical assistance in some contexts. Under the old Chandler Act, the SEC provided a lengthy analysis of the proposed reorganization plan in large cases. This function has been removed, but current bankruptcy law authorizes the court to appoint an examiner to provide objective, expert assistance.[73] The courts have accepted the invitation; in recent cases, examiners have prepared voluminous reports whose conclusions shape the outcome of the case. In *Caesar's*, the examiner's report appears to have catalyzed the reorganization. Now, as in the 1930s, the court also has a democracy-furthering role. The court can disqualify the votes of creditors that have a conflict of interest, for instance, and, as Melissa Jacoby points out, they can take steps to enhance the perceived fairness of the process.

Whether the current level of oversight is sufficient is a matter of debate. The gamesmanship of sophisticated distressed debt investors has brought warnings about ominous phenomena like "empty voting" and the "empty

71 *See* KARL POLANYI, THE GREAT TRANSFORMATION 73 (1957) ("To allow the market mechanism to be the sole director of the fate of human beings . . . would result in the demolition of society.").

72 *See* 11 U.S.C. § 506(b) (2012) (providing that the court determines claims); 11 U.S.C. § 1129 (2012) (determining when a court may confirm a plan).

73 11 U.S.C. § 1104(c) (2012); *see also* Jonathan C. Lipson, *Understanding Failure: Examiners and the Bankruptcy Reorganization of Large Public Companies*, 84 AM. BANKR. L.J. 1, 51 (2010) (examining "[t]he claim that professionals might impede requests for and appointments of examiners").

core."[74] Other recently expressed concerns echo the complaints of the 1930s, when the perception that corporate reorganization did not have sufficient adult supervision and the surge of support for progressive reforms prompted a dramatic enhancement of governmental oversight. As we have already noted—and not dissimilarly to the pattern of the 1930s—a party today has a good chance of short circuiting judicial discretion by presenting its transaction as a fait accompli. As in the 1930s, bankruptcy professionals sometimes seem to be the principal beneficiaries of the bankruptcy process.

Nor do the similarities end there. A blue-ribbon panel has recently rolled out a lengthy list of mostly technical proposed bankruptcy amendments.[75] In its nearly four-hundred page report, the American Bankruptcy Institute commission advocates dozens of reforms, much as the forebears of the National Bankruptcy Conference did in the 1930s. It is not hard to imagine these technical reforms getting swept up in a progressive or populist wave, as did the reorganization reforms of the 1930s. Whereas the key advocate of the earlier reforms, William O. Douglas, came from the SEC, his most likely successor currently resides in Congress: Senator Elizabeth Warren.[76] Both were law school bankruptcy professors before going to Washington.

Senator Warren has in fact recently cosponsored legislation that goes well beyond the ABI's reform proposals. The Warren proposal would upend current bankruptcy practice by curbing corporate debtors' ability to file for bankruptcy in New York and almost completely banning them from filing in Delaware.[77] The reform would force corporate debtors to file in their local jurisdictions. Other similarly dramatic proposals can be found in the existing literature. Some have advocated that the claims of hedge funds and other distressed debt traders be limited to the amount they paid for their debt. This would chill the trading of claims, thus counteracting the expansion of consensual transactions. A populist package might also restrict the fees of bankruptcy lawyers and financial advisors.

---

74 *See* Henry T.C. Hu & Bernard Black, *Equity and Debt Decoupling and Empty Voting II: Importance and Extensions,* 156 U. PA. L. REV. 625, 732-35 n.190 (2008) (describing "empty voting" and related issues); Baird & Rasmussen, *supra* note 42, at 690 ("An 'empty core' exists when three or more parties cannot reach a stable agreement with each other because some other agreement always exists that at least one party prefers.").

75 COMM'N TO STUDY THE REFORM OF CHAPTER 11, AM. BANKR. INST., FINAL REPORT AND RECOMMENDATIONS 6 (2014).

76 For a discussion of intellectual links between the two, see David A. Skeel, Jr., *Vern Countryman and the Path of Progressive (and Populist) Bankruptcy Scholarship*, 113 HARV. L. REV. 1075, 1079 (2000).

77 Bankruptcy Venue Reform Act of 2018, S. 2282, 115th Cong. § 2 (2018); *see also* Katy Stech Ferek, *Bill Aims to Make Bankrupt Companies File for Protection Closer to Home*, WALL ST. J. (Jan. 8, 2018), https://www.wsj.com/articles/bill-aims-to-make-bankrupt-companies-file-for-protection-closer-to-home-1515444161 [https://perma.cc/L5RA-V5FF] ("The bill, if passed, would mark one of the biggest shifts in corporate bankruptcy history, sending cases to courts across the country.").

It is of course possible that sweeping reform will not materialize and there will be limited legislative change in the near future—or, indeed, no change at all. Either way, bankruptcy judges will continue to serve as the principal check on the arrangements devised by the parties, and we expect the overriding theme to be recurrence rather than permanent transformation.

Whatever the future brings, the odds are high that participants in this Symposium will figure prominently in the next phase of corporate bankruptcy history. The bankruptcy scholars who agreed to convene with us in Philadelphia are extraordinary. When future financial historians try to make sense of whatever happens next, we hope they will hone in on this Symposium in their search for clues.

*   *   *   *   *