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CHAPTER XI APPROACHES ITS 'TEENS*

BENJAMIN WEINTRAUB† AND HARRIS LEVIN‡

Chapter XI of the Bankruptcy Act, commonly known as "Arrangements,"¹ was enacted in 1938 and now has almost twelve years of accumulated experience.² Of course, the economic boom of the war years and the short post-war prosperity resulted in very little Chapter XI, or, for that matter, bankruptcy experience.³ But the fiscal year 1949 showed a marked increase in the cases. The spiral of bankruptcy activi-

* An earlier article appeared in 18 N. Y. U. L. Q. REV. 375 (1941), entitled *The Third Year of Arrangements Under the Bankruptcy Act: Crossroads and Signposts*, by the writers of this article and Samuel Singer, B.S. 1936, College of the City of New York; LL.B. 1939, New York University School of Law, formerly an editor of the New York University Law Quarterly Review. Mr. Singer was a member of the Armed Forces of the United States and was killed in action in 1943 during the Italian Campaign.

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¹ 52 STAT. 905-916 (1938), 11 U. S. C. §§ 701-799 (1946). The 1938 amendments to the Bankruptcy Act are also popularly known as the Chandler Act. The Sections of Chapter XI are numbered from 301-399 of the Bankruptcy Act. Citations to the sections of this chapter hereafter will refer solely to the section numbers of the Bankruptcy Act.

² See address of Judge John C. Knox, Chief Judge, Southern District of New York, to N. Y. Credit Men's Ass'n., in 21 REF. J. 112 (1947) where he states in part: "Should it come to pass that the District Court will be inundated with bankruptcies, it is comforting to know that we are fairly well equipped to withstand the flood. The Chandler Act of 1938 is now at our disposal. In bringing about the drafting and enactment of that legislation, your Association played a creditable and influential role. While the statute, like many others, is not letter perfect, the courts have found it to be a tool that is both workable and reasonably efficient. It is the outgrowth of the administrative difficulties and the expensive character of the original 77-B proceedings. In enacting the Chandler Act, Congress, as it were, divided insolvencies into different categories and in doing this, the National legislature was well advised. The provisions of law by which the various types of insolvencies may now be handled admit of greater flexibility in administering individual cases. In addition, administration expenses are less costly than they once were.

"Insolvent business establishments most frequently seek relief under the Arrangement proceedings that are covered by Chapter XI of the Bankruptcy Act."

³ See the annual report of the director of the Administrative Office of the U. S. Courts, dated September, 1949, which presented the following data, at page 15, as to bankruptcy and Chapter XI business in the courts for the fiscal year commencing 1942 and ending for the fiscal year 1949: ". . . The number of cases filed in 1949 was 26,021, compared with 13,170 in 1947. The cases involving substantial assets and requiring the greatest amount of time on the part of the referees, (which are generally involuntary cases and cases under the relief chapters of the Bankruptcy Act) increased in a marked degree in the two years in comparison with prior years. . . ."

ty is obviously upward.⁴ Pre-war experience, consisting of approximately three years, was not an adequate index as to the efficacy of Chapter XI to provide the relief it was designed to furnish. Today sufficient experience has been amassed to form an opinion as to the soundness of the statute. The proceeding has met in this short period of time with encomiums from judges,⁵ referees,⁶ lawyers,⁷ accountants,⁸ business and credit men.⁹ They have all found in its operation a means and method whereby the individual or small corporation has been able to rehabilitate itself and again to start a new economic existence.

The heart and pulse of the entire system is its administration before the referees in bankruptcy.¹⁰ The Act provides¹¹ that upon the filing of the petition, the judge may refer the proceeding to a referee in bank-

⁴ *Id.*, Chart 13 and Exhibit B14, in which the director states: "The number of bankruptcy cases filed in the district court continues to increase. Chart 13 shows the cases commenced annually for the last 44 years. A double top in 1932 and 1935, the aftermath of the depression, was followed by a downward trend. This changed in 1941 to an abrupt decline which reached a low in 1946. Since that time the curve has been upward and for each of the last two years, the increase over the previous year was about 40 percent. . . ." *But see* headline of *N. Y. Times*, Dec. 26, 1949, p. 1, col. 4, "Sawyer Predicts Good Times in '50."

⁵ See 22 *REF. J.* 121 *et seq.* (1948) statements of U. S. Circuit Judges Charles E. Clark and John Biggs, Jr., U. S. District Judges Lindley, Hincks, Wilkin and McCulloch. Judge Clark states at p. 121: "The Bankruptcy Act needs no elaboration now, when it has become so completely a part of the fabric of American national life. When we consider how such comparatively recent innovations as corporate reorganizations through the bankruptcy power have now become a settled feature for our economy, we may perhaps wonder how our country went so long without the beneficent powers and privileges of the Act."

⁶ *Id.* at p. 113, Referee Samuel C. Duberstein; at p. 120, Referee Carl D. Friebohn.

⁷ *Id.* at p. 118, Benj. Wham and W. Randolph Montgomery; at p. 119, Carroll A. Teller; at p. 121, Jacob I. Weinstein; at p. 124, David W. Kahn; and at p. 126, Archie H. Cohen.

⁸ *Id.* at p. 115, Charles S. J. Banks.

⁹ *Id.* at p. 126, Henry H. Heymann.

¹⁰ See address of Mr. Justice Harold C. Burton, 24 *REF. J.* 4, where he states in part: "It is a privilege for me to bring to you the greetings of the Supreme Court of the United States and its grateful appreciation of the services of the referees in bankruptcy of the nation. You render a great and unique service to the country and to the bar and the bench in general. As Judge Biggs so well said, you are 'on the firing line,' and we appreciate the great number of cases that you handle and which never reach us. It is only occasionally that we get a bankruptcy case. When we do, I want you to know that we welcome the referee's opinion, if he has written one. We know, that he has been closer to the facts and witnesses than anybody else, and it is of great value to us to have his written appraisal of the facts and of the law in the light of his special familiarity with the practical application of it."

"I am glad to pay tribute to the referees in bankruptcy as a group. Among the great but unsung services of the federal judiciary are those rendered by the referees in bankruptcy. Their services are little advertised and are little known by the many people who are neither bankrupt nor engaged in bankruptcy practice."

ruptcy and the proceeding then is conducted before the referee until its completion. Most of the opinions, therefore, in Chapter XI proceedings, are opinions which are rendered by the referees, and, for the most part, remain unreported.¹²

Moreover, the referee's courtroom is the laboratory for experimentation. It is there that the experiments have been tried and the Act has been found to be a satisfactory answer to the problems of the small businessman who is beset with financial reverses and cannot meet his obligations as they mature.¹³ The opportunity is presented to freeze these obligations or to scale them down, with the consent of the creditors, and to work out plans which are best suited for the financial rehabilitation of the particular debtor. Each debtor has his own problems, and each of these problems requires a plan based upon a number of factors, depending generally upon whether a composition settlement or an extension of time to pay the debt, is the desired plan. A sound approval of the chapter is found in the proposed amendments which now do not concern themselves with a structural revision of Chapter XI, but point towards a strengthening of its operations.¹⁴

Chapter X¹⁵ or Chapter XI

The choice of chapters is generally not a difficult one. Ordinarily, the classification will depend on the existence of a public interest in the reorganized corporation. Such interest is considered to exist if a large number of securities is held by the public.¹⁶ It follows as a corollary

¹² Sec. 331 provides: "The judge may refer the proceeding to a referee." This has become the established practice in the Southern District of New York.

¹³ The American Bankruptcy Reports which reported bankruptcy cases exclusively, including the opinions of referees, were discontinued in 1945. Commerce Clearing House, Inc. has continued publishing loose leaf binders containing current decisions of referees.

¹⁴ See address of Judge Knox, note 2 at p. 112 *supra*, where he states in part: "Prior to the advent of the Chandler Act, small manufacturers and even storekeepers who got into financial difficulties were faced with heavy expense and involved proceedings, entirely out of line with the importance of such insolvencies. Today, however, this is no longer, required. Under Chapter 11, the ordinary commercial debtor—upon full compliance with the statute—may extend the time within which to pay his unsecured obligations, or he may, if it be desirable, scale down his unsecured debts. One beneficent feature of Chapter 11 is that it gives jurisdiction to the court, in which a petition is filed, to deal with the debtor's property wherever it may be found. The court is thus enabled, with a minimum of confusion, to effect a speedy and economical composition of the debtor's liabilities, and at the same time, adequately protect the creditor body."

¹⁵ See *Senate Judiciary Committee's Confidential Subcommittee Print No. 1*, (Aug. 25, 1949) on H. R. 3111, §§ 31-41, 81st Cong., 1st Sess., (1949).

¹⁶ 52 STAT. 883 (1938), 11 U. S. C. §§ 500-676 (1939). The sections of Chapter X are numbered from 101-276 of the Bankruptcy Act. Citations to the sections of this chapter hereafter will refer solely to the section numbers the Bankruptcy Act.

¹⁶ SEC v. U. S. Realty & Improvement Co., 310 U. S. 434 (1940).

that corporations with stock or bond issues outstanding to the public, will be big in size, i.e., assets, liabilities and subsidiary corporations. Chapter X offers the proper machinery for the reorganization of such corporations.

By this process of inclusion, it should follow that the class of corporations excluded, i.e., small corporations with no public interest, would not avail themselves of the Chapter X proceedings, but would seek reorganization under Chapter XI.¹⁷ For the most part, the formula has been followed in practice, but the choice of chapters does not lend itself to algebraic certitude.

Early in the history of the Chandler Act, the choice of chapters brought the *U. S. Realty & Improvement*¹⁸ case to the Supreme Court. In that case the debtor having 900,000 shares of capital stock listed on the New York Stock Exchange, held by 7,000 stockholders, and having assets of \$7,076,515.00 and liabilities of \$5,051,416.00, filed a petition under Chapter XI. It sought only a modification of unsecured obligations, having by other means arranged for the reclassification of its stocks and bonds.

The SEC contended that Chapter X was the "exclusive procedure"¹⁹ for the debtor and that Chapter XI is "peculiarly adapted to the speedy composition of debts of small individual and corporate enterprises."²⁰ The Court noted that neither chapter contained any "definition or classification that will enable us to say that a corporation is small or large, its security holders few or many, or that its securities are 'held by the public' so as to place the corporation exclusively within the jurisdiction of the court under one chapter rather than the other."²¹

The Court concluded that although the District Court had jurisdiction, nevertheless it should have dismissed the proceeding, suggesting to the debtor that it initiate, if so advised, a new proceeding under Chapter X.²²

¹⁷ Sec. 130 provides as a condition for seeking relief under Chapter X the following: "Every petition shall state—

(7) the specific facts showing the need for relief under this chapter and why adequate relief cannot be obtained under chapter XI of this Act. . . ."

¹⁸ See note 16, at p. 442, *supra*.

¹⁹ *Id.* at p. 444.

²⁰ *Id.* at p. 447.

²¹ *Id.* at p. 447.

²² See bill, H. R. 3111, note 14, *supra*. This bill includes amendments to Chapter XI. The proposed Sec. 328 would obviate the necessity of filing a new petition. It reads as follows: "At any time prior to the first date set for the meeting of creditors to be held pursuant to section 334 of this Act, the judge may, upon application of any party in interest, and upon such notice to the debtor, to the Securities and Exchange Commission, and to such other persons as the court may direct, if he finds that the pro-

To the uninitiated, this determination may seem to be without any resultant harm to the debtor. But the apparent advantage gained in filing under Chapter XI, instead of Chapter X, is the absence in the former of powerful safeguards, in the public interest, i.e., the mandatory trustee,²³ and the intervention of the SEC.²⁴

An analysis of three current cases throws additional light on the problem. In the *Motty-Eitington* case²⁵ a debtor filed a petition under Chapter XI where its assets were listed at \$15,075,337.02 and its liabilities at \$16,321,609.36. A comparison of assets and liabilities between this company and the U. S. Realty & Improvement reveals that the latter's assets and liabilities were little more than a third as great. However, there was no public interest involved in the former and its petition was held properly filed under Chapter XI. Size alone, therefore, is not the determining factor.

In the *Ovington* case,²⁶ a debtor having assets of \$230,000 and liabilities of \$361,944, filed a petition under Chapter X. Its 500 stockholders held common, preferred and participating preferred, for a total capitalization of \$40,000.²⁷ The pendency of the proceeding makes it difficult to visualize the ultimate purpose of the debtor, but it would appear, if no reclassification or adjustment of the stock is contemplated, that the corporation could properly have filed its petition under Chapter XI.²⁸

The third is the *Bacon Clement* case.²⁹ Three creditors filed an involuntary petition against the debtor under Chapter X. There was no public interest involved, and no stock readjustment. A voluntary petition under Chapter X would have been impossible. The reason given for filing a Chapter X proceeding was that the debtor refused to file

ceedings should have been brought under chapter X of this Act, enter an order dismissing the proceedings under this chapter, unless within such time as the judge shall fix the petition be amended to comply with the requirements of chapter X for the filing of a debtor's petition or a creditors' petition under such chapter be filed. Upon the filing of such amended petition, or of such creditors' petition, and the payment of such additional fees as may be required to comply with section 132 of this Act, such amended petition or creditors' petition shall thereafter, for all purposes of Chapter X of this Act, be deemed to have been originally filed under such chapter."

²³ Sec. 156.

²⁴ Sec. 208.

²⁵ Bankruptcy Docket No. 84866 (S. D. N. Y. 1944).

²⁶ *In re Ovington's Gift Shop, Inc.*, Bankruptcy Docket No. 86839 (S. D. N. Y. 1950).

²⁷ *Daily News Record*, Jan. 26, 1950, p. 17, col. 4.

²⁸ See note 16 at p. 452 *supra*. One of the many differences between the chapters is that chapter X concerns itself with the reorganization of a class of securities and chapter XI only with unsecured debts.

²⁹ *Bacon Clement Corp.*, Bankruptcy Docket No. 86880 (S. D. N. Y. 1950).

voluntarily under Chapter XI.³⁰ Strangely enough, there is no parallel provision in Chapter XI, as there is in Chapter X, for the filing of an involuntary petition.

However, a continuance of this practice will result in the reverse of the *U. S. Realty & Improvement Co.* situation, namely, corporations finding themselves in Chapter X, when they should be in Chapter XI. Not only is the procedure too cumbersome in Chapter X for such a corporation, but it puts another burden upon the district judge.³¹ This jurisdictional reason militates against the soundness of the Act's failure to permit the filing of an involuntary Chapter XI.³²

Initiating the Proceeding

The financial upheaval experienced by a debtor is a gradual process. Very often capital is depleted and losses which are damaging to the business accrue, without his realizing that the time for rehabilitation is at hand. The spark which touches things off is too often the presence of the sheriff with an execution against his property. The need is then compelling to procure a stay which will prevent the sale of his business.

In the present state of the Act, the machinery necessary for rehabilitation consists of many schedules and voluminous data.³³ The proceeding is instituted under Chapter XI by the debtor's filing a petition stating either that he is insolvent or that he is unable to pay his debts as they mature.³⁴ The petition must be accompanied by a statement of the executory contracts of the debtor, the schedules of his assets and liabilities in detail and a statement of affairs.³⁵ Furthermore, local rules³⁶ prescribe additional papers to be executed with the filing of the petition.³⁷ Compliance must also be made with the General Orders

³⁰ See §§ 130-131.

³¹ Chapter X provides for the judge's supervision of the proceeding. Whereas, in Chapter XI the judge may assume jurisdiction, nevertheless, in practice he always refers the proceeding to a referee in bankruptcy.

³² No provision is contained in H. R. 3111, note 14, *supra*, for such an amendment, which seems to be a necessity, if proceedings which properly belong under Chapter XI are not to find themselves in Chapter X.

³³ Five copies of petitions and schedules, all executed as originals, and three copies of statement of affairs, all executed as originals, are required to be filed. This requirement is combined from contents of Sec. 7 of Bankruptcy Act (3 copies of petitions and schedules and statement of affairs), Section 394 (1 copy of petition and schedules) and General Order of the Supreme Court No. 48 (1 copy of petition and schedules).

³⁴ § 323.

³⁵ § 324.

³⁶ See Bankruptcy Rules XI-1 to XI-10, S. D. N. Y. (1941).

³⁷ *Id.* Rule XI-3 provides for the submission of an affidavit if the debtor desires to continue his business. In general, this affidavit requires the submission of a number of

of the Supreme Court.³⁸

Obviously the collating of all this data puts a heavy burden on the debtor in his race against time and the sheriff. The question then arises as to how much of this material is necessary for the initiation of the proceeding and how much can be postponed to a later date. An aid to celerity in the filing of a voluntary petition in bankruptcy is contained in Section 7 of the Bankruptcy Act which grants an extension of time for the filing of the schedules and does not require the filing of the statement of affairs until at least five days prior to the first meeting of creditors.³⁹

This makes for a speedy filing of a voluntary petition in bankruptcy in order to avoid preferential dispositions of the bankrupt's property in bankruptcy proceedings. No similar provision is contained in arrangement proceedings. Nor does it seem that Section 302,⁴⁰ making applicable to Chapter XI proceedings the provisions of Chapters I-VII, could be invoked, because of the apparent conflict between Sections 7 and 324. But, the exigencies of the situation have given rise to a procedure.

This is illustrated by a case which arose in the Southern District of New York, *In re Sydenham Hospital, Inc.*⁴¹ There, a membership hospital corporation filed a petition under Chapter XI and at the same time, submitted a separate petition and order to the judge, stating that it had not been able to obtain sufficient information with which to pre-

facts which will inform the court and creditors as to the probability of the debtor's continuing his business at a profit.

³⁸ Sec. 30 of the Bankruptcy Act provides: "All necessary rules, forms and orders as to procedure and for carrying the provisions of this title into force and effect shall be prescribed and may be amended from time to time by the Supreme Court of the United States." In accordance with this authority, the Supreme Court has promulgated General Order 48, which applies to Chapter XI proceedings. This order makes applicable the General Orders in Bankruptcy to Chapter XI insofar as they are not inconsistent. The Supreme Court has prescribed a form of debtor's petition, schedules and statement of affairs. These are known as official forms, numbers 1, 2 and 3 respectively.

³⁹ Sec. 7 reads in part: ". . . *Provided*, That the court may for cause shown grant further time for the filing of such schedules if, with his petition in a voluntary proceeding or with his application to have such time extended in an involuntary proceeding, the bankrupt files a list of all such creditors and their addresses; (9) file in triplicate with the court at least five days prior to the first meeting of his creditors a statement of his affairs in such form as may be prescribed by the Supreme Court; . . ."

⁴⁰ Sec. 302 provides in part: "The provisions of chapters I to VII, inclusive, of this Act shall, insofar as they are not inconsistent with or in conflict with the provisions of this chapter, apply to proceedings under this chapter. For the purpose of such application, provisions relating to 'bankrupts' shall be deemed to relate also to 'debtors'. . ."

⁴¹ Bank. Docket No. 86649 (S. D. N. Y. 1949).

pare its schedules and requested that it be permitted to file its petition without schedules and asking for additional time to file its schedules and statement of affairs. There were more than 300 creditors in that proceeding and the actual work of verifying the amounts due to each, as well as the preparation of all the other details required by the schedules was a tremendous task requiring the services of an accountant.⁴²

Nevertheless, in order to obviate any question as to the power of the court to grant such an extension, an amendment has been proposed to Section 324⁴³ which should answer the need for immediate filing.

Venue

To a debtor who has to appear in court, meet with his creditors, and operate his business, venue is an important consideration. The chapter contains an express provision.⁴⁴ The same venue which controls the filing of ordinary bankruptcy petitions applies in arrangements, namely, that the petition must be filed in the jurisdiction where the debtor has had his principal place of business or where he has resided for the preceding six months.⁴⁵

This preference of residence or principal place of business generally creates no difficulty. But problems do arise in connection with parent-subsidiary corporations. Is the same forum available for both parent and subsidiary? In *In re Olson Marine Supplies*,⁴⁶ a corporation engaged in the ship chandlery business in the City of New York filed a petition under Chapter XI, Section 322. Its principal place of business

⁴² *Id.* Referee Herbert Loewenthal authorized the retention by the debtor-in-possession of an accountant for the purposes of assisting in this laborious task. See also *In re Sword Line, Inc.*, Bank. Docket No. 85727 (S. D. N. Y. 1948), where Referee Irwin Kurtz granted several extensions of time to the debtor to file schedules because of the difficulty involved in their preparation.

⁴³ See note 14 *supra*, § 34: "The petition shall be accompanied by—(1) a statement of executory contracts of the debtor, and the schedules and statement of affairs, if not previously filed: *Provided, however*, That if the debtor files with the petition a list of his creditors and their addresses and a summary of his assets and liabilities, the court may, on application by the debtor, grant for cause shown further time, not exceeding ten days, for filing the statement of the executory contracts and the schedules and statement of affairs. . . ."

⁴⁴ Sec. 322 provides: "If no bankruptcy proceeding is pending, a debtor may file an original petition under this chapter with the court which would have jurisdiction of a petition for his adjudication."

⁴⁵ Section 2 grants the court power to "(1) Adjudge persons bankrupt who have had their principal place of business, resided or had their domicile within their respective territorial jurisdictions for the preceding six months, or for a longer portion of the preceding six months than in any other jurisdiction. . . ."

⁴⁶ Bankruptcy Docket No. 85957 (S. D. N. Y. 1948).

was in the City of New York and it had branches operated by three wholly owned subsidiaries, each of which carried on a similar business in Virginia,⁴⁷ Maryland⁴⁸ and Pennsylvania,⁴⁹ respectively. The parent corporation filed its petition in the Southern District of New York, as did each of the subsidiaries. Prior to filing, creditors in Virginia had attached the property of the Virginia corporation and creditors in Maryland had attached the property of the subsidiary operating there. The referee granted a stay against these attaching creditors. They, however, filed an answer, contesting the jurisdiction of the court on the ground that the petition was not properly filed in the Southern District of New York, each of the subsidiaries having been incorporated in the particular state where it was operating and not at its home office. The question finally became moot as the result of a plan of arrangement which was satisfactory to the creditors, but great harm could have been done if the court had sustained the contention of these creditors and held that the principal place of business of each of the subsidiaries was not in the Southern District of New York. Under such circumstances the principal officers of the debtor would have had to be present in each of four jurisdictions, and four courts would have controlled the debtor's destiny, with none having a definitive plan for the whole.

To avoid the possibility of an adverse ruling on parent-subsidiary corporations, the chapter should be amended to grant the subsidiary the option of filing either in its own jurisdiction or in that of its parent. Such a provision would parallel that contained in Chapter X.⁵⁰

Transfer of a case where it has been brought in an improper jurisdiction is also authorized by the provisions of the Bankruptcy Act.⁵¹ The importance of transferring cases to other courts of bankruptcy instead of dismissing them is obvious. Dismissal would often entail a preferential lien being restored, to the detriment of general creditors. No similar provision is contained in Chapter XI; it would appear that a transfer is authorized under the provisions of Section 302, but the Act should be amended to relieve any doubt on that score.

Furthermore, removal from one jurisdiction to another should be permitted where the wrong jurisdiction has been invoked, or the interest

⁴⁷ Bankruptcy Docket No. 85967 (S. D. N. Y. 1948).

⁴⁸ Bankruptcy Docket No. 85971 (S. D. N. Y. 1948).

⁴⁹ Bankruptcy Docket No. 85973 (S. D. N. Y. 1948).

⁵⁰ Sec. 129 reads: "If a corporation be a subsidiary, an original petition by or against it may be filed either as provided in Section 128 of this Act or in the court which has approved the petition by or against its parent corporation."

⁵¹ Sec. 2(19) reads: "Transfer cases to other courts of bankruptcy."

of creditors requires it. This is the procedure under Chapter X⁵² and the same reasons prevail for a similar provision under Chapter XI.

Compensation of Creditors' Committees

The chapter provides for the appointment of a committee by the creditors⁵³ and the payment of "the actual and necessary expenses" of the committee, its attorneys or agents.⁵⁴ These sections were interpreted in the *Haytian* case,⁵⁵ which clarified the statute by enunciating the following basic principles:

1. The chapter contemplates a single creditors' committee, with advisory power only, to act without compensation.⁵⁶

2. The expenses allowable to the committee are to be "limited to those incurred by it in passing judgment upon the plan and in making that judgment known to the debtor and the creditors for appropriate action by him or them."

3. No compensation is allowable to the individual members of the committee.

4. Attorneys or agents retained by the committee shall only be compensated for services within the compass of the committee's own duties.

5. Expenses incurred prior to the committee's appointment under Section 338 are not compensable.⁵⁷

A comparison between the holding of the *Haytian* case and provisions contained in Chapter X show a wide variance, both as to the time compensation commences and the services for which compensation is allowable. Section 242 provides for compensation for services rendered by committees, their attorneys and agents. Section 243 provides for the type of services which are compensable, namely:

1. Services contributing to the confirmation or refusal of confirmation of the plan of reorganization.

2. Services which are beneficial in the administration of the estate.

Such differences as the single committee in Chapter XI as against many in Chapter X, and the refusal to compensate committeemen in Chapter XI, are readily understandable, as being dictated by the size

⁵² Sec. 118 reads: "The judge may transfer a proceeding under this chapter to a court of bankruptcy in any other district, regardless of the location of the principal assets of the debtor or its principal place of business, if the interests of the parties will be best served by such purpose."

⁵³ § 338.

⁵⁴ § 337 (2).

⁵⁵ *Lane v. Haytian Corp. of America*, 117 F. 2d 216, (2d Cir. 1941).

⁵⁶ *Id.* at p. 220.

⁵⁷ *Id.* at p. 221.

of the respective proceedings.⁵⁸ But, the time of commencement of service in Chapter XI and the type of service compensable are not realistic. It is axiomatic that the work of the committee begins the moment a debtor calls a meeting of its creditors and the committee is formed.

A proposed amendment to Section 337 endeavors to achieve reform.⁵⁹ It would compensate the committee's agents, provided the committee was selected or approved by a majority (in amount of claims) of unsecured creditors, excluding those who could not vote under Section 44 of the Act. Although the remedy is sound, its application seems fraught with difficulty. This committee would be chosen out of court; its representation of a majority in amount of unsecured claims may often fall short by one or two claims in constituting an approved majority. Furthermore, since Section 338⁶⁰ is to be amended to omit the election of a committee, no time limit is fixed for the approval of this committee and it may very well have to wait until shortly before confirmation of a plan to ascertain whether it has the blessing of a majority in amount of claims.

A more practical approach would be to allow payment of the necessary costs and expenses to the so-called unofficial committee, provided a majority of its members are appointed as the official committee. In practice there is generally only one unofficial committee and this becomes the official committee. This was the situation in *In re Max Fishman, Inc.*,⁶¹ where the unofficial committee, having become the official committee, sought compensation for its attorney and accountant. The claim was disallowed because of the absence of an appropriate provision in the chapter. The same factual situation with regard to committee personnel was also present in the *Fisher* case.⁶²

⁵⁸ See *Nassberg v. Rockwell*, 172 F. 2d 554, (2d Cir. 1949).

⁵⁹ See note 14 *supra*, § 33, which requires the debtor to deposit the money necessary to pay the costs and expenses of the proceedings and the actual and necessary expenses incurred before or after the filing of the petition under this chapter by any committee of creditors, which is ". . . selected or approved by a majority in claims of unsecured creditors, who would not be disqualified by section 44 of this Act to participate in the appointment of a trustee, in such amount as the court may allow: *Provided, however*, That in fixing any such allowances the court shall give consideration only to the services which contributed to the arrangement confirmed or to the refusal of confirmation of an arrangement, or which were beneficial in the administration of the estate, and the proper costs and expenses incidental thereto. . . ."

⁶⁰ *Id.* § 34.

⁶¹ 27 F. Supp. 33 (S. D. N. Y. 1939).

⁶² *In re Fisher Dress Corporation*, 33 F. Supp. 157 (S. D. N. Y. 1939).

Fair and Equitable: Words of Art

A condition precedent to the confirmation of any arrangement is a finding by the court that the plan is fair and equitable.⁶³ A similar condition is contained in Chapter X.⁶⁴ This phrase was first characterized as "words of art," which had acquired a definitive meaning in reorganization proceedings by Mr. Justice Douglas in *Case v. Los Angeles Products Lumber Co.*⁶⁵

There a petition for reorganization under former Section 77B of the Bankruptcy Act⁶⁶ had been filed. The debtor was a holding company which owned six subsidiaries; its assets were valued at \$900,000; liabilities to bondholders amounted to \$3,800,000. The corporation was obviously insolvent. Notwithstanding this condition, the plan of reorganization provided for the retention by stockholders of an interest in the corporation of 23% of the value of the corporation.⁶⁷ The Court, therefore, held that this participation by stockholders did not meet the requirement that creditors are entitled to priority over stockholders in the property of an insolvent corporation.⁶⁸

Case v. Los Angeles Products Lumber Co. reaffirmed and crystallized the doctrine enunciated in *Northern Pacific Railway Co. v. Boyd*⁶⁹ and a host of equity receivership proceedings, including railroad reorganizations. The doctrine has become a fixed principle of corporate reorganization for the protection generally of the interests of priority groups against management.⁷⁰ Its extension to Chapter XI proceedings resulted from a dictum in the *U. S. Realty & Improvement Co.* case,⁷¹

⁶³ Sec. 366 reads in part: "The Court shall confirm an arrangement if satisfied that—
 (1) the provisions of this chapter have been complied with;
 (2) it is for the best interests of the creditors;
 (3) it is fair and equitable and feasible, . . ."

⁶⁴ Sec. 221 reads in part: "The judge shall confirm a plan if satisfied that—
 (1) the provisions of article VII section 199, and article X of this chapter have been complied with;

(2) the plan is fair and equitable, and feasible; . . ."

⁶⁵ 308 U. S. 106, 115 (1939).

⁶⁶ 48 STAT. 911, 11 U. S. C. 207 (1934).

⁶⁷ See note 65, at p. 119, *supra*, where the court stated: "Hence even if all the assets were turned over to the bondholders, they would realize less than 25 per cent on their claims. Yet in spite of this fact they will be required under the plan to surrender to the stockholders 23 per cent of the value of the enterprise."

⁶⁸ *Id.* at p. 123 where the rule is characterized as a "rule of full or absolute priority."

⁶⁹ 228 U. S. 482 (1913).

⁷⁰ See note 65, at p. 129, *supra*; and Note, 35 Cornell L. Q. 412 as to later cases discussing the absolute priority doctrine (1950).

⁷¹ See note 65, at p. 119, *supra*, where the court stated: "'Fair and equitable' taken from Section 77B and made the conditions of confirmation, under both Chapter X or Chapter XI are 'words of art' having a well understood meaning in reorganizations in

where the court traced its history to Section 77B. It must, however, be remembered that all corporations, regardless of size, had no choice of sections but of necessity had to reorganize under Section 77B.⁷² During the same period of time, individuals seeking a composition or an extension of time, availed themselves of Section 74. Historically, Chapter XI stems not from its foster parent, 77B, but from the old composition Sections 12 and 74.⁷³

An amendment to Section 366,⁷⁴ is designed to eliminate the "fair and equitable" features. This would have the effect of eliminating the application of the *Los Angeles* and *Boyd* doctrines as applied in the *U. S. Realty* case. Since an arrangement is designed primarily for a small business or individual, and public interest is not involved,⁷⁵ the elimination of this doctrine is only a practical recognition of what takes place in most arrangement proceedings. Management, which initiates the proceeding under Chapter XI, generally obtains either a compromise of obligations or an extension of time to pay them. In most instances, management remains in control and is the essence of any arrangement. Creditors are not in a position to furnish new management which is of a personal nature and which very often depends for its existence upon the activities of one or two of the principals.⁷⁶ The determination, therefore, in Chapter XI proceedings is more soundly based upon whether the plan "is in the best interests of creditors."⁷⁷ Under this interpretation, the problem is resolved as to what creditors would receive in

equitable receiverships and under 77B which is incorporated in the structure of both Chapters X and XI."

⁷² 48 STAT. 911, 11 U. S. C. 207 (1934).

⁷³ See Note, 17 N. Y. U. L. Q. REV. 254 (1940).

⁷⁴ See note 14, section 37, *supra*, which reads in part: "The court shall confirm an arrangement if satisfied that—

- (1) the provisions of this Chapter have been complied with;
- (2) it is for the best interests of creditors and is feasible; . . .

"Confirmation of an arrangement shall not be refused because the interest of a debtor or, if the debtor is a corporation, the interests of its stockholders or members will be preserved under the arrangement even though the arrangement or the order confirming the arrangement does not provide for payment in full of the claims of creditors."

⁷⁵ See note 16, at p. 449 *supra*, where the Supreme Court held as follows: "While we do not doubt that in general, as will presently appear more in detail, the two chapters were specifically devised to afford different procedures. The one adapted to the reorganization of corporations with complicated debt structures and many stockholders, the other to composition of debts of small individual business and corporations with few stockholders. . . ."

⁷⁶ See *In re Sarlo Sales Co.*, Docket No. 86153 (S. D. N. Y. 1949) where Referee Stephenson refused to confirm a plan under Chapter XI of the Bankruptcy Act where the debtor had offered a settlement of 20% in cash, but confirmed the same plan where the debtor offered 25% in cash.

⁷⁷ Sec. 366.

liquidation or at a sale of the assets as against what they would receive on confirmation of the plan.⁷⁸

In the *Nathanson* case,⁷⁹ a Chapter XI proceeding, the referee found that the sum necessary to confirm the arrangement was \$9,000 and that the amount that would be realized upon a liquidation of the assets would be \$7,500, which would be less than what the debtor was offering under the plan. Therefore, he found the arrangement to be in the best interests of the creditors, although he denied confirmation on other grounds. This was a 25% settlement with unsecured creditors. Based on the same theory, he held that the plan, since it would give creditors more than at liquidation, was fair and equitable. Going concern value and the absolute priority doctrine were not considered.

In the *Krieger* case⁸⁰ a debtor filed an arrangement under Chapter XI. Objections were filed on the grounds that it was not in the best interests of creditors and that it was not fair and equitable. The court found that liabilities were \$20,500, assets \$36,000. The compromise would cost the debtor approximately \$6,000. The court held that the test was not whether creditors would receive less in liquidation, but that the creditors should receive equitable treatment, citing the *Los Angeles* case. The court's interpretation of equitable treatment was that the creditors should receive at least what the assets were really worth.⁸¹

This reasoning is supported by the decision in *In re John Lucas*.^{81a}

⁷⁸ See *Fleischmann & Divine, Inc. v. Wolfson Dry Foods Co.*, 299 Fed. 15 (5th Cir. 1924), where the Court held that a 40% offer to creditors was unfair in view of the fact that all of the assets would bring sufficient to warrant a payment of 60% to creditors. This proceeding was under the provisions of Sec. 12 of the Bankruptcy Act of 1898.

⁷⁹ *In re Nathanson*, 50 Am. B. R. (N. S.) 465, (Ref. Ind. 1941).

⁸⁰ *In re H. Krieger & Co.*, 40 Fed. Supp. 340 (D. C. Conn. 1941).

⁸¹ *Id.* at p. 342, where Judge Hincks states: "But on the other hand it does not necessarily follow that an arrangement, to be equitable, must provide for payments, in cash and on time, which shall in the aggregate fully equal the value of the assets. For necessarily a debtor who has just turned over all his property to the court for administration is limited in any cash payments which he can offer by what he can borrow. Of course, he can seldom obtain a loan for full value of a mercantile business which is his only basis for credit. And if successful in obtaining a loan, he must reserve enough cash for working capital, until the balance can be paid in cash to old creditors on the confirmation of a plan. Whether he can properly be required to supplement cash payments with deferred payments necessarily depends upon the prospective income of the business."

^{81a} Bankruptcy Docket No. 86495 (S. D. N. Y. 1950). References to pages are to those of the unreported opinion. The decision in this proceeding was rendered on April 25, 1950. This article was submitted for publication to the CORNELL LAW QUARTERLY on March 1, 1950. Because of its importance in substantiating the point enunciated in this subdivision of the article, the writers asked QUARTERLY for permission to amend the galley proof.

The debtor filed a voluntary petition in bankruptcy. Thereafter, he filed a petition under Section 321 of the Bankruptcy Act. His original plan proposed to pay creditors 20% in cash; it was later amended to 25% in cash. The second amended plan was accepted by a majority of the debtor's creditors.

However, specifications of objections were filed by one creditor to the confirmation of the amended plan, claiming among other things, that the amended plan was not "fair and equitable" and not "for the best interests of the creditors". Referee Schofield, however, confirmed the amended plan. The objecting creditor then filed a petition to review the order of the referee.

Judge Conger in reviewing the order of the referee commented on the fact that the fair value of the debtor's assets was the sum of \$24,000 and that the cost of financing the arrangement proceeding was the sum of \$22,489.70 exclusive of administration expenses.

Commenting on the plan, the judge held at page 5:

The final specifications concern themselves with whether the plan is 'fair and equitable' and whether it is 'for the best interests of the creditors.' These are conditions precedent to confirmation and are contained in Section 366 of the Bankruptcy Act. 'Fair and equitable' have come to have a fixed meaning in Chapter X reorganizations. (See *Section 221 of the Bankruptcy Act* and *Case v. Los Angeles Products Lumber Co.*, 308 U. S. 106 (1939)). Its principle has generally been urged to protect priority interests against management.

But, notwithstanding its inclusion in Chapter XI proceedings, the Courts have more often treated a Chapter XI composition settlement on the basis of the fair value of the assets. Thus, *In re H. Krieger & Co.*, 40 F. Supp. 340, 342, the Court held that equitable treatment under Chapter XI meant that the debtor was to pay creditors not 'less than the assets of the estate are really worth.'

The proceeding is treated as it should be, either as an extension of unsecured obligations or as a composition. The present amendment to Section 366 (H. R. 3111, 81st Cong., 1st Sess. June 7, 1949) takes realistic cognizance of the fact that 'fair and equitable' in Chapter XI proceedings must mean as Judge Hincks stated in the Krieger case, *supra*, that creditors shall receive what the assets are really worth. See 24 Referees' Journal 34. . . .

The court found the amended plan to be "fair and equitable" and "for the best interests of the creditors." The judge dismissed the specifications of objections to the amended plan of arrangement, and affirmed the order of the referee.

The cases show the difficulty of administering the absolute priority doctrine in Chapter XI proceedings. To paraphrase Mr. Justice Douglas, the "words of art" in Chapter XI proceedings, are "the best interests of the creditors."⁸²

⁸² See Oglebay, *Some Landmark Cases in the Development of the Bankruptcy Act*

Confirmation of the Plan of Arrangement

Section 357 provides that the court may retain jurisdiction of the proceeding.⁸³ One of the difficult questions confronting a debtor in formulating such a plan is whether to include in the plan a provision for jurisdiction by the Court. Obviously, if the debtor offers a plan where creditors are paid a percentage of their claims in cash, there is no need for the retention of jurisdiction. But the flexibility of the various types of plans⁸⁴ provided for in a Chapter XI proceeding, namely, the payment of claims in instalments extending over many years, payment of dividends out of profits in the same or in a newly-organized corporation, supervision by creditors' committees and a host of others, make it a perplexing problem for the debtor. One authority⁸⁵ has gone so far as to hold such a provision generally inadvisable in a plan of arrangement. Problems arising out of such a retention of jurisdiction can be grouped as follows:

(1) Shall debts created after confirmation of the arrangement have priority in a subsequent insolvency over the old debts, including such old priorities as unpaid taxes?

(2) When does the statute of limitations begin running on preferences and fraudulent transfers created after confirmation in a new insolvency proceeding?

(3) Does property acquired after the confirmation pass to the trustee in a subsequent insolvency?

(4) Are the claims of old creditors to be allowed in the new proceeding in their full amounts or in their adjusted amounts?

Two of the leading cases decided by the Court of Appeals for the Second Circuit have discussed these problems. In *Vogel v. Mohawk Electrical Sales Co.*,⁸⁶ the plan of arrangement did provide that the court retain jurisdiction. Creditors filed an involuntary petition on March 25th, 1949. On March 30th, 1949, the debtor petitioned for an

of 1898, 22 REF. J. 105 (1948): "But the statute itself would have been a lifeless system of legal jargon, had not the courts, through the years, breathed into it the living substance of construction and interpretation, adapting the statutory language to situations of reality and even by misconstruction emphasizing the necessity for the changes which are a part of the growth of our law."

⁸³ Sec. 357 reads in part: "An arrangement within the meaning of this chapter may include— . . .

(7) provisions for retention of jurisdiction by the court until provisions of the arrangement, after its confirmation, have been performed."

⁸⁴ Sec. 306 provides, in part: "For the purposes of this chapter, unless inconsistent with the context—(1) 'arrangement' shall mean any plan of a debtor for the settlement, satisfaction, or extension of the time of payment of his unsecured debts, upon any terms, . . ."

⁸⁵ 8 COLLIER, BANKRUPTCY 1085 (14th ed. 1941).

⁸⁶ *Vogel v. Mohawk Electrical Sales Co.*, 126 F. 2d 759, (2d Cir. 1942).

arrangement under Chapter XI, Section 321. It thereafter submitted a plan which was accepted by its creditors, providing for a 30% payment of claims in instalments. The plan provided for a creditors' committee which, among other powers, had the right, in the event of a default, to apply for an immediate liquidation. It also provided that any debts thereafter incurred were to be subordinated to the rights of the original creditors and that the court was to retain jurisdiction of the debtor until the last instalment was paid. There was a further provision in the plan that the creditors' committee was to hold the certificates of stock of the debtor and that the committee would elect directors to act in the place of the former directors.

After confirmation, the committee took charge of the debtor's business and continued it in the debtor's name, buying necessary supplies from creditors. The debtor failed to meet its instalments and the committee then applied to the court for a liquidation of the assets. An order of adjudication was entered on January 10th, 1940. In the course of the proceedings a creditor named Vogel filed a claim demanding payment as an expense of administration on the theory that he had dealt with the debtor after the confirmation of the plan of arrangement and while the court still held jurisdiction.

Judge Learned Hand, writing for the Court, held that new creditors after confirmation would be entitled to be paid their claims ahead of the old creditors, as the underlying theory was to enable the debtor to continue in business in such a manner as to vie with his competitors, which he could not possibly do unless the new creditors felt that in the event of a liquidation they would come ahead of the old creditors.⁸⁷ Judge Learned Hand concluded that Vogel's debt was not an expense of administration, because the period of administration ended with the entry of the order of confirmation, but that the claimant was entitled to a priority over and above all the old debts.

In *Seedman v. Friedman*,⁸⁸ Judge Clark wrote the opinion of a

⁸⁷ *Id.* at p. 761, where judge Learned Hand represents this situation in this descriptive language: ". . . for the underlying theory must be that he shall have a chance to establish himself again and that he cannot have unless he can do business upon equal terms with his competitor. It is idle to ask him to fight his way with one arm tied. Yet if any new creditors who sell to him must accept the possibility that if he fails to perform the 'arrangements', they must share with the old creditors (not to the extent of the payments fixed in the composition which presumably have been so far scaled down as to be supportable, but to that of the whole sum of the old debts) they are extremely likely not to deal with him at all. Unless he can assure them as to the amount of his actual liabilities without a contingent addition of the old debts, he will start with a handicap in a race which he has already once lost. . . ."

⁸⁸ *Seedman v. Friedman*, 132 F. 2d 290 (2d Cir. 1942).

unanimous court. The Humpty Dumpty Auto Stores, Inc. filed a petition under Chapter XI, Section 322 of the Bankruptcy Act in January, 1940. A plan of arrangement was agreed upon which provided for deferred monthly payment to the creditors. The plan also provided for a creditors' committee, giving the said committee authority to liquidate the corporation upon a default in the aforementioned payments and also giving the committee supervision over the debtor's conduct of its business. The court retained jurisdiction after confirmation for the purposes of carrying out the provisions of the arrangement. In the course of the proceeding Seedman had entered into a contract with the debtor to purchase its assets. The sale was to be consummated in accordance with the provisions of Section 44 of the Personal Property Law of the State of New York, commonly known as the Bulk Sales Law. After the contract had been signed, but before the sale could be consummated, a petition was presented to the District Court to adjudicate the debtor a bankrupt because of a fraud practiced in the confirmation of the plan of arrangement. The Court adjudicated the debtor a bankrupt. Seedman then filed a claim for breach of contract, claiming priority. The trustee moved to expunge this.

Judge Clark emphasized that the retention of jurisdiction did not mean that the court was exercising a supervision and control of the debtor such as is exercised during the pendency of the proceeding before confirmation.⁸⁹ The court held the claim allowable and that the debtor had authority to enter into such a contract. Judge Clark also held the claim was entitled to a priority over the debts provable in the arrangement proceeding.

Section 377⁹⁰ describes the procedure to be followed where adjudication takes place if the court has retained jurisdiction after confirmation. The section does not define the status of claims which accrue subsequent to confirmation.

Another one of the amendments proposed to the Bankruptcy Act would add a new Section 379⁹¹ so as to clarify the status of such claims

⁸⁹ *Id.* at p. 294, where Judge Clark stated: "The court, however, was without authority to exercise a continuous act of control over the debtor's business. . . ."

⁹⁰ Sec. 377 reads in part: "Where the court has retained jurisdiction after the confirmation of an arrangement and the debtor defaults in any of the terms thereof or the arrangement terminates by reason of the happening of a condition specified in the arrangement the court . . . shall—

(2) where the petition has been filed under section 322 of this Act, enter an order adjudging the debtor a bankrupt, and directing that bankruptcy be proceeded with pursuant to the provisions of this Act. . . ."

⁹¹ See note 14, Sec. 41, *supra*, which reads in part: "Chapter XI of such Act, as amended, is amended by renumbering 'Sec. 379' to read 'Sec. 380' and 'Sec. 380' to read 'Sec. 381', and by inserting in its numerical order the following section:

where confirmation of a plan of arrangement is followed by an adjudication in bankruptcy. It also clarifies the title to property vested in the trustee. Subdivision (1) gives the trustee title to all property as of the date of the entry of the order directing bankruptcy. This disposes of the question of whether newly acquired property is vested in the trustee and seems to be a logical solution of the entire problem.

This amendment provides that all unsecured debts incurred after the confirmation of the arrangement shall share on a parity with the prior unsecured debts of the same classes and that the prior unsecured debts shall be reduced to the amount provided for them in the arrangement. In other words, if a plan provides for the payment of creditors on the basis of 30% of their provable claims and thereafter the plan is confirmed and bankruptcy ensues, the new creditors' claims will be provable for the full amount but the claims of the old creditors will be provable only to the extent to which they were reduced in the previous arrangement. There is a saving clause which provides "unless and except as otherwise provided in the arrangement or in the order confirming the arrangement." The debtor may, therefore, provide in his plan of arrangement that in the event of any such liquidation his new creditors after confirmation shall be paid first before old unsecured creditors. This may have the effect of allowing a debtor to obtain credit such as Judge Learned Hand anticipated would be necessary to enable the debtor to continue in business.

The new subdivision 3 of Section 379 would make applicable the provisions of Chapters I to VII inclusive and would make the date of

'Sec. 379. Where, after the confirmation of an arrangement, the court shall enter an order directing that bankruptcy be proceeded with—

(1) the trustee shall, upon his appointment and qualification, be vested with the title to all the property of the debtor as of the date of the entry of the order directing that bankruptcy be proceeded with;

(2) the unsecured debts incurred by the debtor after the confirmation of the arrangement and before the date of the entry of the final order directing that bankruptcy be proceeded with shall, unless and except as otherwise provided in the arrangement or in the order confirming the arrangement, share on a parity with the prior unsecured debts of the same classes, provable in the ensuing bankruptcy proceeding, and for such purpose the prior unsecured debts shall be deemed to be reduced to the amounts respectively provided for them in the arrangement or in the order confirming the arrangement, less any payment made thereunder; and

(3) the provisions of chapters I to VII, inclusive, of this Act, shall, insofar as they are not inconsistent or in conflict with the provisions of this section, apply to the rights, duties and liabilities of the creditors holding debts incurred by the debtor after the confirmation of the arrangement and before the date of the final order directing that bankruptcy be proceeded with, and of all persons with respect to the property of the debtor, and for the purposes of such application, the date of bankruptcy shall be taken to be the date of the entry of the order directing that bankruptcy be proceeded with.'"

the order directing that bankruptcy be proceeded with the date of bankruptcy. It is a practical solution of the difficult problem as to what would be considered the date of bankruptcy in the event of an adjudication after confirmation of a plan of arrangement. In effect, it treats the proceeding as if it were an entirely new one dating from the date of the entry of the order confirming the plan of arrangement; the date of the entry of an order directing bankruptcy becomes the date of bankruptcy.

Conclusion

The Bankruptcy Act has gone a long way since the first Act of 1800 and the social theory of bankruptcy has progressed considerably since the Act of 1898.⁹² The accent is on rehabilitation⁹³ and on giving an honest debtor a second opportunity to make a livelihood instead of upon punitive measures.⁹⁴

There is hardly a type of small business or institution that has not availed itself of the relief afforded by the Act. There have not only been commercial enterprises, as varied as brick manufacturers,⁹⁵ a chain of industrial caterers,⁹⁶ shoe stores,⁹⁷ restaurants,⁹⁸ manufacturers

⁹² See Weisman, *Some Chapters of Bankruptcy History: From the Bankruptcy Clause to the Act of 1898*, 22 REF. J. 99 (1948).

⁹³ The concept of the arrangement proceedings as a social law which ministers to an ailing business, finds support in the concept of maturity as to law. Functionally, Chapter XI has reached its maturity. This concept of maturity is discussed in OVERSTREET, *THE MATURE MIND* (1949). At page 196, Prof. Overstreet states: "Traditionally, the American . . . has enjoyed politics maturely; trying to match laws to ideals, tinkering the social mechanism back into running order when it has broken down, . . . his political maturity is expressed . . . in laws to protect the helpless and to increase opportunities for growth. . . ." See also opinion of Judge Conger, note 81a, *supra*, where he states at page 8: ". . . Certainly the best interests of creditors cannot be stretched beyond the point where the debtor pays fair value for his assets. To hold otherwise, would he to ignore the rehabilitation features of Chapter XI. See address of Judge Knox in 21 REF. J. 112 (1947). . . ."

⁹⁴ See Duberstein, *Bankruptcy—Its Future!*, 22 REF. J. 113: "The Supreme Court has declared unequivocally that the Constitution's bankruptcy power is flexible enough to serve the social and economic needs of ever-changing generations and conditions. The underlying definition of bankruptcy has changed from 'liquidation' to 'rehabilitation'. It is the present purpose of bankruptcy laws to conserve a debtor's business, including good-will, rather than the sacrifice by forced sale; this aim should be furthered to an even higher degree in the future. Handling these matters requires special training, knowledge of varied laws, business skill and human relationships. Fortunately, however, these qualifications are possessed in great measure by our body of Referees, who are performing a creditable service in the administration of the subject of bankruptcies and it is of greatest importance to our Country, creditors and debtors."

⁹⁵ *In re Terry Brick Corp.*, Bankruptcy Docket No. 86631 (S. D. N. Y. 1949), where Referee Arthur J. Doran continued in possession of its business a debtor and its six wholly owned subsidiaries.

⁹⁶ *In re Franky-Swanky, Inc.*, Bankruptcy Docket No. 46803 (E. D. N. Y. 1946)

of kitchen equipment,⁹⁹ ship chandlers,¹⁰⁰ and steamship lines,¹⁰¹ but also institutional concerns that have been confronted with financial difficulties. In *In the Matter of the Gardner School, Inc.*,¹⁰² a girls' preparatory school filed a petition under Chapter XI of the Bankruptcy Act and sought to work out an arrangement with its creditors.¹⁰³

In *In the Matter of Sydenham Hospital, Inc.*,¹⁰⁴ a petition under Chapter XI was filed by a hospital in the City of New York because of its inability to pay its obligations as they matured. The hospital could not operate profitably and the plan of arrangement provided that the fixtures and equipment be sold to the City of New York for a stipulated sum of money which would be distributed to creditors in accordance with their priorities. While this plan was being consummated, the debtor was authorized by Referee Herbert Loewenthal to continue a lease with the City, whereby the latter took over operating functions. A valuable service to the community was thereby continued without interruption.

Chapter XI is no longer an experiment but an accomplishment of high esteem in the economic life of the country. Approaching its twelfth year, it has managed to supply a need in financial rehabilitation. Its maturity has been accelerated not only by the sound and practical decisions of the court, but, "even by misconstruction emphasizing the necessity for changes. . . ."¹⁰⁵ It is a living doctrine having a close

where Referee Sherman D. Warner confirmed a plan of arrangement of industrial cafeterias.

⁹⁷ *In re* David Kay Shoe Co., Bankruptcy Docket No. 86771 (S. D. N. Y. 1949) where Referee Robert P. Stephenson continued in possession of its business a debtor operating shoe concessions in numerous department stores in many eastern states.

⁹⁸ *In re* Enduro Restaurant Corp., Bankruptcy Docket No. 47871 (E. D. N. Y. 1949) where Referee Louis J. Castellano confirmed a plan of arrangement of a debtor operating a restaurant in the Borough of Brooklyn.

⁹⁹ *In re* Master Sales Corp., Bankruptcy Docket No. 47898 (E. D. N. Y. 1949) where Referee Samuel C. Duberstein confirmed a plan of arrangement of a debtor engaged in manufacturing kitchen equipment.

¹⁰⁰ *In re* Carl M. Rissotto Co., Inc., Bankruptcy Docket No. 86182 (S. D. N. Y. 1949) where Referee John E. Joyce continued in possession a ship chandler operating in New York and Virginia.

¹⁰¹ *In re* S. S. Sandy Hook Co., Docket No. 86624 (S. D. N. Y. 1949) where Referee Irwin Kurtz continued in possession a debtor operating a steamship between New York and New Jersey.

¹⁰² Bankruptcy Docket No. 86454 (S. D. N. Y. 1949) where Referee Loewenthal continued the debtor in possession of its business.

¹⁰³ See N. Y. *Times*, Nov. 23, 1949, p. 32, col. 4, for some of the historical background and social significance in this 92-year-old school which endeavored to work out a plan of arrangement with its creditors.

¹⁰⁴ Bankruptcy Docket No. 86649 (S. D. N. Y. 1949).

¹⁰⁵ See note 82 *supra*.

relation to the reality of our economic existence.¹⁰⁶ "For the underlying theory must be that he shall have a chance to establish himself again."¹⁰⁷

¹⁰⁶ See statement of Morris L. Ernst, N. Y. Times, Dec. 30, 1949, p. 16, col. 1, where, commenting on New York State's divorce laws, he states: "I do not mean that law must always be the exact concomitant of prevailing customs. But the lag cannot continue as it is today. . . ."

¹⁰⁷ See note 87 *supra*.