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# Written Testimony

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## "Exploring Chapter 11 Reform: Corporate and Financial Institution Insolvencies; Treatment of Derivatives"

**Subcommittee on Regulatory Reform, Commercial and Antitrust Law**
**Committee on the Judiciary**
**United States House of Representatives**

**2141 Rayburn House Office Building**

**March 26, 2014**

Chairman Bachus, Ranking Member Johnson, and members of the Subcommittee, thank you for the opportunity to testify today. My name is Michelle Harner, and I am a Professor of Law and the Director of the Business Law Program at the University of Maryland Francis King Carey School of Law. Prior to my academic career, I was a Partner at the law firm of Jones Day in Chicago, Illinois, and I practiced primarily in the corporate restructuring area. As an academic, my research and scholarship focuses on corporate governance and corporate restructuring issues. I am honored to appear before you today.

I have been asked to testify today in my capacity as Reporter for the ABI Commission to Study the Reform of Chapter 11 (the "Commission"). As such, my comments today are on behalf of the Commission and not in my personal capacity. The Commission was formed in 2012 to study the utility of chapter 11 of the U.S. Bankruptcy Code. The Commission comprises twenty of the nation's leading practitioners, judges, and academics.[1] It was constituted by the American Bankruptcy Institute, the largest multi-disciplinary, non-partisan organization dedicated to research and education on matters related to insolvency. The University of Maryland Francis King Carey School of Law received a grant from the American Bankruptcy Institute and the Anthony H.N. Schnelling Endowment Fund to support my research and service as Reporter.[2]

Chapter 11 of the Bankruptcy Code facilitates the resolution of financial distress primarily in the business context.[3] It emerged as a compromise to chapter X and chapter XI of the U.S. Bankruptcy Act of 1898 (introduced by the Chandler Act of 1938), under which large, public business debtors were subject to the mandatory appointment of

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[1] A list of the Commissioners is attached at ***Appendix A***.
[2] The ABI has committed approximately $300,000 to fund the overall study and reform project.
[3] The Commission and the study are not addressing issues unique to the resolution of an individual debtor's financial distress under chapter 11.

a bankruptcy trustee and oversight by the Securities and Exchange Commission and smaller business debtors essentially negotiated a resolution with their creditors.[4] After almost forty years of experience under chapter X and chapter XI of the prior Bankruptcy Act, policymakers and practitioners agreed that reform was needed, resulting in one business bankruptcy chapter—chapter 11 of the Bankruptcy Code.[5] After more than thirty years of experience under chapter 11, many practitioners and commentators again agree that it is time for reform.[6]

The Commission is conducting a thorough investigation of business bankruptcies and the potential need for reform. The Commission is still in its study and deliberation phase of the process, and it is not yet putting forth any conclusions or recommendations. The Commission does not anticipate doing so until the study phase is completed and the Commissioners have fully vetted all relevant issues. Accordingly, my testimony today will summarize: (i) the potential need for reform of chapter 11 of the existing Bankruptcy Code; (ii) the Commission's study process; and (iii) certain testimony and research received to date by the Commission on reform issues.

***The Potential Need for Reform***

The Bankruptcy Code has served us well for many years. Nevertheless, today's financial markets, credit and derivative products, and corporate structures are very different than what existed in 1978 when the Bankruptcy Code was enacted. Companies' capital structures are more complex and rely more heavily on leverage; their asset values are driven less by hard assets (e.g., real estate and machinery) and more by services,

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[4] *See*, *e.g.*, DAVID A. SKEEL, JR., DEBT'S DOMINION: A HISTORY OF BANKRUPTCY LAW IN AMERICA (2001) (reviewing history of the Bankruptcy Code); Donald R. Korobkin, *Rehabilitating Values: A Jurisprudence of Bankruptcy,* 91 COLUM. L. REV. 717 (1991) (same); Charles Jordan Tabb, *The History of the Bankruptcy Laws in the United States*, 3 AM. BANKR. INST. L. REV. 5 (1995) (same); Daniel J. Bussel, *Coalition-Building Through Bankruptcy Creditors' Committees*, 43 UCLA L. REV. 1547, 1557-58 (1996) (same and discussing components of chapter X and chapter XI of the Bankruptcy Act). *See also* SEC v. Am. Trailer Rentals Co., 379 U.S. 594, 603–606 (1965) (discussing the Chandler Act of 1938); CHARLES WARREN, BANKRUPTCY IN UNITED STATES HISTORY (1935) (reviewing early history of Bankruptcy Code).

[5] Elizabeth Warren, *Bankruptcy Policymaking in an Imperfect World*, 92 MICH. L. REV. 336, 371–73 (1993) (explaining that "[o]ne of the key reasons for the adoption of the 1978 Code was the widespread perception that the old Code was unworkable").

[6] *See* Richard Levin & Kenneth Klee, *Rethinking Chapter 11*, 2012 INT'L INSOLVENCY INST., *available at* http://www.iiiglobal.org/component/jdownloads/finish/337/5966.html. *See also* Stephen J. Lubben, *Some Realism About Reorganization: Explaining the Failure of Chapter 11 Theory*, 106 DICK. L. REV. 267 (2001); Douglas G. Baird & Robert K. Rasmussen, *Chapter 11 at Twilight*, 56 STAN. L. REV. 673 (2003); Harvey R. Miller & Shai Y. Waisman, *Does Chapter 11 Reorganization Remain a Viable Option for Distressed Businesses for the Twenty-First Century?*, 78 AM. BANKR. L.J. 153 (2004); Harvey R. Miller & Shai Y. Waisman, *Is Chapter 11 Bankrupt?*, 47 B.C. L. REV. 129 (2005); James H. M. Sprayregen et al., *Chapter 11: Not Perfect, but Better than the Alternative*, AM. BANKR. INST. J., Oct. 2005, at 1; Harvey R. Miller, *Chapter 11 in Transition—From Boom to Bust and into the Future*, 81 AM. BANKR. L.J. 375 (2007).

contracts, and intangibles; and both their internal business structures (e.g., their affiliates and partners) and external business models are more global. In addition, claims trading and derivative products have changed the composition of creditor classes. These developments are not necessarily unwelcome or unhealthy, but the Bankruptcy Code was not designed to rehabilitate companies in this environment.

Moreover, anecdotal evidence suggests that chapter 11 has become too expensive (particularly for small and middle market companies) and is no longer achieving certain policy objectives such as stimulating economic growth, preserving jobs and tax bases at both the state and federal level, or helping to rehabilitate viable companies.[7] Some suggest that more companies are liquidating or simply closing their doors without trying to rehabilitate under the federal bankruptcy laws.[8] Some suggest that companies are waiting too long to invoke the federal bankruptcy laws, which limits restructuring alternatives and may lead to premature sales or liquidations.[9] Still others suggest that the system continues to work well enough.[10] These issues are at the core of the Commission's study. As explained below, the Commission's process was designed to explore the new environment in which financially distressed companies operate and to determine what is—and is not—working as effectively as possible.

***The Commission's Study Process***

The Commission has undertaken a methodical study of chapter 11 of the Bankruptcy Code. Over 250 individuals (as either Commissioners, committee members, or hearing witnesses) who work in or are affected by corporate insolvencies have been involved in this study process. The Commission has strived to include all perspectives, ideologies, and geographic and industry segments.

The Commission has met on a regular basis since January 2012. During these meetings, the Commission has, among other things, discussed issues perceived as potential problems in chapter 11, reviewed recent developments in the case law and practice norms, and developed an effective process for identifying, researching, and analyzing chapter 11 as a whole. As explained below, the Commission has used an advisory committee structure and numerous public field hearings to amass the information and research it requires to critically analyze chapter 11 and consider any reform measures.

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[7] *See*, *e.g.*, Stephen J. Lubben, *What We "Know" About Chapter 11 Cost is Wrong*, 17 FORDHAM J. CORP. & FIN. L. 1 (2012) (reviewing literature and presenting empirical data to contradict common perceptions of bankruptcy costs).
[8] *See*, *e.g.*, Douglas G. Baird & Robert K. Rasmussen, *The End of Bankruptcy*, 55 STAN. L. REV. 751, 777-85 (2002) (discussing decrease in traditional stand-alone reorganizations).
[9] *See*, *e.g.*, Michelle M. Harner & Jamie Marincic Griffin, *Facilitating Successful Failures,* 66 FLA. L. REV. ___ (forthcoming 2014) (analyzing literature and presenting results of empirical survey on, among other things, timing of bankruptcy filings).
[10] *See*, *e.g.*, Stuart C. Gilson, *Coming Through a Crisis: How Chapter 11 and the Debt Restructuring Industry Are Helping to Revive the U.S. Economy*, 24 J. APPLIED CORP. FIN. 23 (Fall 2012).

*The Advisory Committees*. To launch its study, the Commission identified thirteen broad study topics to facilitate a detailed analysis of the various components of chapter 11. These study topics are: administrative expense claims and other pressures on liquidity; avoiding powers (e.g., preferences and fraudulent conveyances); bankruptcy-remote entities and bankruptcy proofing; distributional issues under plans; executory contracts and unexpired leases; financial contracts, derivatives, and safe harbors; financing issues; governance and supervision of cases; labor and benefits issues; multiple entities and corporate groups; procedural and structural issues under plans; role of valuation; and sales in chapter 11.[11] The Commission then enlisted the volunteer service of over 150 of the profession's very talented and dedicated judges, lawyers, financial advisors, academics, and consultants to serve on advisory committees for each of the study topics.[12]

The advisory committees began their work in April 2012. The Commission provided each advisory committee with a preliminary assessment containing initial study questions for its general topic area. Each advisory committee devoted (and some continue to devote) significant time to researching and evaluating the study questions. The advisory committees met either in-person or telephonically on a frequent basis, reviewing their research and debating the issues. The advisory committees engaged in this work for approximately eighteen months and submitted research reports on most topics to the Commission in December 2013.

The Commission then held a three-day retreat in February 2014 to meet with each advisory committee and discuss the research reports. At the retreat, the advisory committees presented their reports and highlighted complex and nuanced issues for the Commission, and Commissioners actively engaged in a direct dialogue with committee members. The Commission also used the forum to begin integrating the study topics and reconciling overlapping issues. The retreat and the work of the advisory committees leading up to the retreat have been informative and very helpful to the Commission in this process. The Commission currently is reviewing the entire body of work produced by the advisory committees and conducting follow up research and analysis on a variety of issues.

The Commission also formed an international working group consisting of leading practitioners and academics from twelve different countries. The working group

[11] The Commission has asked the financial contracts, derivatives, and safe harbors advisory committee to consider related issues involving systemically important financial institutions and the chapter 14 proposal developed by Professor Thomas Jackson and his colleagues. It also has deferred the work of the multiple entities and corporate groups advisory committee until a later point in the process.

[12] The names and affiliations of members of the advisory committees are listed at the Commission's website: www.commission.abi.org. Two of the witnesses appearing before the Subcommittee today are members of the financial contracts, derivatives, and safe harbors advisory committee—Seth Grosshandler (Co-Chair of the advisory committee) and the Honorable Christopher S. Sontchi.

is studying targeted questions posed by the Commission and the advisory committees to provide a comparative analysis of the relevant issues.

*The Field Hearings*. The Commission held its first public hearing in April 2012 at the House of Representatives, Committee on the Judiciary, Rayburn House Office Building, Washington, D.C. Since that time, the Commission has held fifteen public field hearings in eleven different cities: Boston, Las Vegas, Chicago, New York, Phoenix, San Diego, Tucson, Philadelphia, Austin, Atlanta, and Washington, D.C. In these hearings, almost ninety individuals have testified.[13] The testimony at each of these hearings has been substantively rich and diverse. The hearings have covered a variety of topics including chapter 11 financing, general administrative and plan issues, governance, labor and benefits issues, priorities, sales, safe harbors, small and middle market cases, valuation, professional fees, executory contracts (including commercial leases and IP licenses), trade creditor issues, and avoiding powers reform. Transcripts and videos of the hearings, and the related witness statements, are available at the Commission's website: www.commission.abi.org. A summary of the hearing topics is attached at ***Appendix C***.

Several common themes emerged from the field hearings. First, most witnesses acknowledged that chapter 11 cases have changed over time.[14] These changes include a perceived: increase in the number and speed of asset sales under section 363 of the Bankruptcy Code,[15] decrease in stand-alone reorganizations, decrease in recoveries to unsecured creditors,[16] and increase in the costs associated with chapter 11.[17] Second, the

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[13] The names and affiliations of these witnesses are listed at ***Appendix B***.

[14] *See* Bryan Marsal, Statement to the Commission, Hearing, October 26, 2012 (NCBJ Transcript pp. 15-19), *available at* http://commission.abi.org ("There is a gradual erosion of the underlying public principle of the Code which was to preserve jobs and maximize value through rehabilitation.").

[15] *See* Gerald Buccino, Statement to the Commission, Hearing, November 3, 2012 (TMA Transcript p. 19), *available at* http://commission.abi.org. ("When sales occur too quickly before the rehabilitative process, the yield to pre-petition creditors is diminished."); Michael Richman, Statement to the Commission, Hearing, October 26, 2012 (NCBJ Transcript p. 20), *available at* http://commission.abi.org (recommending that section 363 sales should be modified so that courts can restrain hasty sales and better monitor expedited sales).

[16] *See* Paul Calahan, Written Statement to the Commission for the May 21, 2013 Hearing, *available at* http://commission.abi.org ("The Code and the economic environment have made it more difficult for unsecured creditors to realize fair payment of their claims… A voice for unsecured creditors is clearly needed and provides valuable insight to the court and other parties."); Joseph McNamara, Written Statement to the Commission for the May 21, 2013 Hearing, *available at* http://commission.abi.org ("A tremendous disparity remains between payment of secured and unsecured claims and some evidence suggests secured creditors with first liens experienced outstanding recoveries, while unsecured recoveries were around 20%, with the median recovery set at 10%.").

[17] *See* John Haggerty, Written Statement to the Commission for the April 19, 2013 Hearing, *available at* http://commission.abi.org (recommending that the level of professionals should be rationalized at the onset of a case and fees and billing should be more transparent and have greater oversight during the process to keep overall costs down).

witnesses who testified on issues relating to small and middle market companies generally opined that chapter 11 no longer works for these companies. Witnesses cited cost and procedural obstacles as common barriers.[18] Third, the witnesses who testified on financial contracts and derivatives generally agreed that the safe harbor protections have been extended to contracts and situations beyond the original intent of the legislation.[19] They did not necessarily agree, however, on appropriate limitations or revisions to the relevant sections of the Bankruptcy Code.[20] Finally, witnesses—even those who were highly critical of certain aspects of chapter 11—all perceived value in the U.S. approach to corporate bankruptcies, including the debtor in possession model.[21]

***The Process Going Forward***

The Commission's study process is winding down, and it will begin deliberations in April 2014. Prior to that time, the Commission and the ABI are co-sponsoring a symposium with the University of Illinois College of Law to address issues relating to secured credit and bankruptcy. This symposium is gathering many of the leading bankruptcy scholars to explore the rights of debtors and secured creditors under state law and the Bankruptcy Code. Many scholars also will address the related Constitutional and public policy issues.[22] The research papers presented at that symposium will inform the Commission's work and appear in the University of Illinois Law Review.

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[18] *See* Hon. Dennis Dow, Written Statement to the Commission for the April 19, 2013 Hearing, *available at* http://commission.abi.org (noting that the complexity, time and costs of the chapter 11 process impose obstacles that small business debtors often cannot overcome); Prof. Anne Lawton, Written Statement to the Commission for the November 1, 2013 Hearing, *available at* http://commission.abi.org ("The Code's small business debtor definition should be simplified."); Gerald Buccino, Statement to the Commission, Hearing, November 3, 2012 (TMA Transcript pp. 7, 15), *available at* http://commission.abi.org ("A one-size-fits-all approach for the Code does not work because smaller businesses have special needs.").

[19] *See* Daniel Kamensky on behalf of Managed Funds Association, Written Statement to the Commission for the October 17, 2012 Hearing, *available at* http://commission.abi.org (asserting that the breadth of safe harbors has had unintended consequences and some courts have held that safe harbors extend to protect one-off private transactions that do not involve financial institutions); Jane Vris, Statement to the Commission, Hearing, May 15, 2013 (NYCBC Transcript p. 9), *available at* http://commission.abi.org ("The original purpose of the safe harbors was to preserve the clearing of payments and delivery within a fair closed system, the protections have now expanded beyond that.").

[20] *See* Hon. James Peck, Statement to the Commission, Hearing, May 15, 2013 (NYCBC Transcript p. 32), *available at* http://commission.abi.org (recommending that judges should have more discretion to determine whether contracts fit the criteria for protection under the safe harbors).

[21] *See* William Greendyke, Written Statement to the Commission for the November 22, 2013 hearing, *available at* http://commission.abi.org (reporting that the membership of the Bankruptcy Law Section of the State Bar of Texas noted that the chapter 11 process still worked, but found it to be more expensive and "faster" than 10 years ago.).

[22] The names and affiliations of the academics presenting at this symposium are listed at ***Appendix D***.

The Commission will devote significant time to reviewing the vast body of research, data, and testimony generated through its two-year study process. It will debate the issues internally and work to build consensus around a set of findings and conclusions. The Commission currently anticipates producing a preliminary report in December 2014.

Although the Commission does not yet know what it ultimately will recommend in that report, it is guided by its mission statement to "study and propose reforms to Chapter 11 and related statutory provisions that will better balance the goals of effectuating the effective reorganization of business debtors—with the attendant preservation and expansion of jobs—and the maximization and realization of asset values for all creditors and stakeholders."

**Appendix A**

ABI Commission to Study the Reform of Chapter 11

D.J. (Jan) J. Baker, Latham & Watkins LLP

Donald S. Bernstein, Davis Polk & Wardwell LLP

Geoffrey L. Berman (*ex officio*), Development Specialists, Inc.

William A. Brandt, Jr., Development Specialists, Inc.

John Wm. Butler, Jr., Skadden, Arps, Slate, Meagher & Flom LLP

Babette A. Ceccotti, Cohen, Weiss & Simon LLP

Samuel J. Gerdano (*ex officio*), American Bankruptcy Institute

Hon. Arthur J. Gonzalez (retired), U.S. Bankruptcy Court, Southern District of New York

Steven M. Hedberg, Perkins Coie LLP

Robert J. Keach (Co-chair), Bernstein Shur

Prof. Kenneth N. Klee, University of California at Los Angeles, School of Law

Richard B. Levin, Cravath, Swaine & Moore LLP

James T. Markus (*ex officio)*, Markus Williams Young & Zimmerman, LLC

Harvey R. Miller, Weil, Gotshal & Manges LLP

James E. Millstein, Adjunct Professor of Law, Georgetown Law Center

Harold S. Novikoff, Wachtell, Lipton, Rosen & Katz

James P. Seery, Jr., River Birch Capital, LLC

Sheila T. Smith, Deloitte Financial Advisory Services LLP

James H.M. Sprayregen, Kirkland & Ellis LLP

Albert Togut (Co-chair), Togut, Segal & Segal, LLP

Clifford J. White III, Director (non-voting), Executive Office for the U.S. Trustees (DOJ)

Bettina M. Whyte, Alvarez & Marsal

Deborah D. Williamson, Cox Smith Matthews Incorporated

## Appendix B

Public Filed Hearing Witness List

Rep. Howard Coble, NC

Hon. Joan Feeney, Bankruptcy Court D. Ma.

Sen. Charles E. Grassley, IA

Prof. Edward I. Altman, New York University, School of Business

Ted Basta, LSTA

John Greene, Halcyon Asset Management LLC

Prof. Edith S. Hotchkiss, Boston College, School of Management

Daniel B. Kamensky, Paulson & Co., Inc. (on behalf of MFA)

A.J. Murphy, Bank of America Merrill Lynch

Lee Shaiman, GSO Capital Partners, Blackstone

Hon. Eugene R. Wedoff, Bankruptcy Court N.D. Ill

John Collen, Tressler, LLP

Howard Brownstein, The Brownstein Corp.

Bryan P. Marsal, Alvarez & Marsal

Michael P. Richman, Hunton & Williams LLP

Brad B. Erens, Jones Day

Craig Goldblatt, Wilmer Hale

Ronald Barliant, Goldberg Kohn Ltd., Bankruptcy Court N.D. Ill. (Ret.)

Hon. Melanie Cyganowski, Otterbourg, Steindler, Houston & Rosen, PC, Bankruptcy Court E.D. N.Y. (Ret.)

Michael Haddad, Newstar Business Credit (on behalf of CFA)

Jonathan N. Helfat, Otterbourg, Steindler, Houston & Rosen, PC (on behalf of CFA)

Richard M. Kohn, Goldberg Kohn Ltd. (on behalf of CFA)

Randall Klein, Goldberg Kohn Ltd.

Robert Katz, Executive Sounding Board Associates, Inc.

Gerald Buccino, Buccino & Associates

Kathryn Coleman, Hughes, Hubbard & Reed

Richard Mikels, Mintz, Levin, Cohn, Ferris, Glovsky and Popeo, P.C.

Danielle Spinelli, Wilmer Hale

J. Scott Victor, SSG Capital Advisors, LLC

William Derrough, Moelis & Company LLC

Mark Shapiro, Barclays Capital

Jennifer Taylor, O'Melveny & Myers LLP

Janet Chubb, Armstrong Teasdale

Hon. Robert D. Drain, Bankruptcy Court S.D.N.Y.

Hon. Gregg W. Zive, Bankruptcy Court D. Nev

Peter S. Kaufman, Gordian Group LLC

Hon. James M. Peck, Bankruptcy Court S.D.N.Y.

Sandra E. Horwitz, CSC Trust Company of Delaware

Eric Siegert, Houlihan Lokey

Prof. David C. Smith, University of Virginia, McIntire School of Commerce

David R. Jury, United Steelworkers

Michael L. Bernstein, Arnold & Porter

Hon. Stephen S. Mitchell, Bankruptcy Court E.D. Va (Ret.)

Joshua Gotbaum. Pension Benefit Guaranty Corporation

James C. Little, Transportation Workers Union

Michael Robbins, Air Line Pilots Association

Deborah Sutor, CWA – Association of Flight Attendants

Robert Roach, International Association of Machinists and Aerospace Workers

Wilbur L. Ross, WL Ross & Co.

Hon. Dennis R. Dow, Bankruptcy Court W.D. Mo.

Hon. Barbara G. Houser, Bankruptcy Court N.D. Tx.

Hon. Pamela Pepper, Bankruptcy Court E.D. Wi.

Daniel F. Dooley, MorrisAnderson

John M. Haggerty, Argus Management

Holly Felder Etlin, AlixPartners

Daniel J, Ehrmann, Alvarez & Marsal

Christopher K. Kiplok, Hughes Hubbard & Reed LLP

Edward Murray, Allen & Overy LLP

Jane L. Vris, Millstein & Co. (on behalf of National Bankruptcy Conference)

Prof. David A. Skeel, University of Pennsylvania, School of Law

Valerie Venable, CCE, Ascend Performance Materials LLC

Kathleen M. Tomlin, CCE, Central Concrete Supply Co., Inc.

Thomas Demovic, CCE, CICP, Sharp Electronics Corp.

Joseph P. McNamara, CCE, Samsung Electronics USA

Paul D. Calahn, CCE, CICP, Cargill, Inc.

Sandra Schirmang, CCE, ICCE, Kraft Foods Global, Inc.

Lawrence C. Gottlieb, Cooley, LLP

Elizabeth I. Holland, Abbell Credit Corporation

David L. Pollack, Ballard Spahr LLP

Robert L. Eisenbach, III, Cooley, LLP

Lisa Hill Fenning, Arnold & Porter

Jeffrey A. Wurst, Ruskin Moscou Faltischek, P.C.

Grant Newton, Association of Insolvency and Restructuring Advisors

Grant Stein, Alston & Bird LLP (on behalf of AIRA)

Prof. Jonathan C. Lipson, Temple University, School of Law

Prof. Daniel L. Keating, Washington University, School of Law

Dennis F. Dunne, Milbank, Tweed, Hadley & McCloy, LLP

William K. Snyder, Deloitte CRG

Brady C. Williamson, Godfrey & Kahn, S.C.

Mark A. Gittelman, PNC Bank

Prof. Anne Lawton, Michigan State University, College of Law

W. Clarkson McDow, United States Trustee, Region 4 (Ret.)

Thomas J. Salerno, Squire Sanders LLP

Prof. George W. Kuney, University of Tennessee, College of Law

Maria Chavez-Ruark, Saul Ewing LLP

Courtney Engelbrecht Barr, Locke Lord LLP (on behalf of IWIRC)

Kathleen M. Miller, Smith, Katzenstein & Jenkins LLP (on behalf of IWIRC)

Prof. Anthony J. Casey, University of Chicago, School of Law

Prof. S. Todd Brown, University of Buffalo, School of Law

William R. Greendyke, Norton Rose Fulbright

Michael R. Rochelle, Rochelle McCullough, LLP

G. Eric Brunstad, Jr., Dechert LLC

Hon. Steven W. Rhodes, Bankruptcy Court D. Mi.

Prof. Jay Westbrook, University of Texas, School of Law

Douglas B. Rosner, Goulston & Storrs, PC

Michael Luskin, Luskin Stern & Eisler LLP

James L. Patton, Jr., Young Conaway Stargatt & Taylor, LLP

## Appendix C

Summary of Field Hearings and Topics of Discussion

The October 17, 2012 field hearing was at held the Loan Syndications and Trading Association (LSTA) annual meeting in New York, New York. The hearing generally covered finance and governance concerns in chapter 11, and witnesses testified on debtor in possession (dip) lending, distressed debt trading, and the role of secured credit. The Managed Funds Association (MFA) testified on various aspects of governance reform, suggesting changes involving the appointment of trustees, the addition of new members to a debtor's board of directors, and the appointment and management of creditors' committees. Representatives from LSTA presented data on the relationship between dip lending and reorganization, and witnesses encouraged the Commission to consider the positive role that distressed debt trading has on the market.

The Commission hosted a roundtable discussion on sales as part of a field hearing on October 26, 2012 during the annual meeting of the National Conference of Bankruptcy Judges (NCBJ) in San Diego, California. During the roundtable, witnesses recommended reviewing the time limits on the section 363 sale process, in particular for small business cases, and with respect to plan exclusivity. Another witness discussed the scope and ambiguity in sales approved under section 363(f) of the Code. Witnesses also spoke more generally on the challenges faced by small and middle market companies using chapter 11, and on potential reforms in credit-bidding and lender control provisions.

On November 3, 2012, the Commission held a field hearing at the Turnaround Management Association's annual meeting in Boston, Massachusetts. During the field hearing, witnesses provided comments on reforming the Federal Rules of Bankruptcy Procedure, the impact of *Stern v. Marshall*, the role of judicial discretion, executory contracts, and DIP lending. Comments from witnesses included: the suggestion that the time to assume or reject non-residential real property was too short; that the speed of a section 363 sale was too quick, diminishing value to pre-petition creditors; and that section 503(b)(9) protections should be abolished. One witness suggested reforms to DIP lending and amending the standard in section 1111(b) in the context of credit-bidding.

The field hearing on November 15, 2012 was held at the annual convention of the Commercial Finance Association (CFA) in Phoenix, Arizona. The primary focus of the field hearing was finance, and the witnesses testified on DIP lending, the use of carve-outs, and challenges to small and medium-size enterprises. The leadership of CFA testified on behalf of their membership and suggested the Commission study the following topics: adequate protection for secured creditors, carve-outs, the inclusion of all contract rights in the definition of secured claims, and the enforceability of inter-creditor agreements. Included among the potential reforms proposed by witnesses were: modifying the Code to allow for the statutory appointment of a sale monitor or examiner; codifying local rules to provide guidance or standards for the court to base its discretion on; clarifying sections 1129 and 1104 of the Code; codifying gifting; providing for the

enforcement of fraudulent conveyance savings clauses; and shifting the burden of proof in preferential transfer claims.

During the ABI Winter Leadership Conference in Tucson, Arizona, the Commission held a field hearing on November 30, 2012. This field hearing centered on finance and governance under chapter 11, in particular the role of creditors' committees, DIP lending, the use of secondary markets, surcharges, and roll-ups. While discussing the use of secondary markets, one witness suggested that the Code should clarify that bad faith does not turn solely upon a creditor's motivation and that bad faith does not exist solely because a creditor took actions that are associated with distressed investing.

The Commission held a field hearing during the VALCON Conference in Las Vegas, Nevada, on February 21, 2013. The field hearing focused on valuation, including: different valuation methodologies; the pros and cons of judicial valuation; and the timing of valuations in chapter 11 cases. Witnesses made a number of suggestions to improve the valuation process used during chapter 11, including the use of the Discounted Cash Flow Analysis over the Market Test, and offering the court, at its election, access to a valuation consultant.

The March 14, 2013 field hearing was held at the spring meeting of the American College of Bankruptcy in Washington, DC. The field hearing centered on labor provisions within the chapter 11 process, in particular sections 1113 and 1114 of the Code and the impact of the proposed Conyers Bill. Recommendations for reform included: eliminating the 14-day time frame for a court hearing on section 1113 and 1114 motions; modifying the test to terminate a defined-benefit pension plan; restoring concessions if unsecured creditors ultimately get paid in full or receive value equal to 100% of their claims; and maintaining the right to self-help. Many of the witnesses felt that payment into pension funds or 401(k) plans should be more strongly enforced and that the labor force should be permitted to participate more actively in a debtor's business plan.

In conjunction with the ABI Annual Spring Meeting in Washington, DC, the Commission held a field hearing on April 19, 2013. This particular field hearing included testimony on professional fees and the challenges of small and middle market companies utilizing the chapter 11 reorganization process. A number of recommendations were made to address the perception of excessive professional fees, including: a guideline in the present billing system that would provide a ceiling for the class' fees as a percentage of total recovery; weekly reports accompanied by memos that explained the firm's prior week's fees and expenses; or other systems that would promote greater transparency, enhance debtor supervision of professionals, and rationalize the level of professionals at the onset. Other witnesses provided insight into the unique challenges that small and middle market companies face in efforts to reorganize under chapter 11 of the Code, like the 300-day deadline for filing a plan and disclosure statement, the section 1129(a) 45-day requirement to confirm a plan, and the application of the Absolute Priority Rule. For comparison purposes, the witnesses offered observations about the increased use of state law alternatives to chapter 11.

As part of the New York City Bankruptcy Conference, the Commission held a field hearing on May 15, 2013 in New York, New York. The focus of the field hearing was the role of financial contracts and derivatives, and the use of safe harbors, in chapter 11 cases. A number of recommendations for reform were proffered by the witnesses, including: tailoring the settlement payment definition to confirm more closely to Congress' original intent; imposing a self-reporting requirement on counterparties exercising safe harbors; allowing the debtor continued access to information from its clearing banks; and providing more protection to the estate's operating assets. In addition, a discussion was held surrounding the appropriateness of a three-day automatic stay for the exercise of safe harbors, the level of judicial discretion that should be granted within the definition and enforcement of safe harbors, and whether a set interest rate should apply to payouts.

The Commission heard from a number of witnesses regarding administrative claims and avoiding powers during its May 21, 2013 field hearing at the National Association of Credit Management conference in Las Vegas, Nevada. During a robust discussion on section 503(b)(9), one witness suggested the inclusion of drop shipment transactions in the protections of that section. A number of witnesses supported changes to the preference statute to afford more protections and defenses to creditors and place more of the burden on trustees and debtors to evaluate preference claims prior to demands. Additionally, witnesses shared that the window for bringing preference actions was too broad and a cost-benefit analysis should be required when evaluating preference demands, demonstrating that pursuing the preference action would provide benefit to the unsecured creditors above the cost to pursue the action.

On June 4, 2013, the Commission held a field hearing on executory contracts, leases, and related intellectual property issues in bankruptcy at the New York Institute of Credit conference in New York, New York. A panel of witnesses represented two distinct and opposite views on the impact and value of the 210-day rule to assume or reject non-residential leases. The witnesses also discussed the treatment of stub rents, a lessee's post-petition obligations under section 365(d)(3), and the definition of adequate assurance of future performance in the context of the assumption and assignment of leases. The panel of witnesses that discussed intellectual property issues offered suggestions to reform section 365(c) to adopt the "Actual Test," and to reform sections 365(g), (n) to adopt the *Lubrizol* decision. Further, the suggestion was made to modernize the definition of patents to include foreign issued patents and clarify change of control provisions.

Another field hearing of the Commission was held on June 7, 2013 in Chicago, Illinois, at the annual meeting of the Association of Insolvency & Restructuring Advisors (AIRA). The field hearing began with a report from AIRA leadership on those issues most concerning to their membership, including the format and detail of disclosure statements, the use of judicial discretion, and the revival of "KERPs." The Commission also heard from two academics regarding the interaction between labor law and the Code,

and the role of governance and the value of information, in particular control discovery, in chapter 11.

The Commission again held a field hearing at the National Conference of Bankruptcy Judges Annual Meeting, which took place on November 1, 2013 in Atlanta, GA. The discourse of this hearing focused on a number of general proposals for reform of the Code, including: the oversight of committee work; the value of a third-party reorganization professional; and the role and selection of a trustee. The Commission also heard from an academic reporting on her study of small business debtors under the current Code and proposals for reform, including modifying the definition of "small business debtor" and eliminating the 45-day plan-confirmation deadline for those debtors.

On November 7, 2013, the Commission held its first field hearing in the third judicial circuit at the 10th Annual Complex Restructuring Program at the Wharton School of Business in Philadelphia, PA. The Commission heard from a number of different witnesses that testified on the role and responsibility of the debtor in possession and other parties in interest, the unique challenges faced in asbestos-related chapter 11 cases, and issues within priority rules, in particular, codifying the new value corollary of the absolute priority rule. One witness focused on reform proposals that would reduce the costs and ease the timetables applicable in small or middle market cases. The Commission also heard testimony on behalf of the International Women's Insolvency and Restructuring Confederation (IWIRC). IWIRC's testimony focused on streamlining the process for asserting section 503(b)(9) claims, including standardizing the forms and procedures for asserting such claims and establishing a timeline in which they must be asserted.

The last field hearing of 2013 for the Commission occurred at the University of Texas/Jay Westbrook Conference in Austin, TX on November 22, 2013. The Commission heard from two representatives of the Bankruptcy Law Section of the State Bar of Texas on the results of an online survey of its members, including general suggestions for reform of the chapter 11 process like standardizing the role and practices of the U.S. Trustee across districts and/or regions, legitimizing the section 363 sale process, and making bankruptcy judges Article III judges. In addition to a number of focused proposals on reform within the Code, the Commission heard testimony regarding two larger issues: the impact of *Stern v. Marshall* and the role venue plays in bankruptcy proceedings.

## Appendix D

Academics Currently Scheduled for April 2014 Symposium

David C. Smith, University of Virginia McIntire School of Commerce

Mark Jenkins, University of Pennsylvania, Wharton School of Business

Michelle M. Harner, University of Maryland, School of Law

Adrian J. Walters, IIT Chicago-Kent, College of Law

Melissa B. Jacoby, University of North Carolina

Edward J. Janger, Brooklyn Law School

Kenneth M. Ayotte, North Western University, School of Law

David G. Carlson, Yeshiva University, School of Law

Gary Holtzer, Weil, Gotshal & Manges LLP

Juliet M. Moringiello, Widener University, School of Law

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

Steven L. Schwarcz, Duke University, School of Law

Edward Morrison, University of Chicago, School of Law

Bruce A. Markell, Florida State University, College of Law

Charles W. Mooney, Jr., University of Pennsylvania, School of Law

Steven L. Harris, IIT Chicago-Kent, College of Law

Charles J. Tabb, University of Illinois, College of Law

Barry E. Adler, New York University, School of Law

Stephen J. Lubben, Seton Hall University, School of Law

Jay Lawrence Westbrook, University of Texas, School of Law