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Bankruptcy Fiduciaries

Christopher D. Hampson

BANKRUPTCY FIDUCIARIES

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Does social enterprise end with insolvency? Is bankruptcy all about the bottom line? The answer to these questions begins with understanding the estate in bankruptcy and the fiduciaries that control its fate. Yet the law of fiduciary duties in bankruptcy is undertheorized, conflicted, and muddled. After almost fifty years of confusion, this Article provides the first comprehensive examination of the nature and source of fiduciary duties in bankruptcy. Although the Supreme Court has intoned "maximize the value of the estate" as a shorthand, I argue that the trustee's duty of obedience in reorganization cases gives rise to a "duty to facilitate a plan" or, as I call it, a "duty to clear runway." I also conclude, based on 28 U.S.C. § 959, that the trustee must observe state law fiduciary duties that would otherwise have governed the debtor outside of bankruptcy. Trustees of benefit corporations, for example, must not pursue money-maximization above all else, but must balance pecuniary interests against the public benefit set forth in the debtor's articles, such as preserving employment, protecting the environment, or supporting the local economy. For their part, creditors and debtors alike have opportunities to advocate for public-minded goals in bankruptcy cases as part of official committees or, in a novel twist, a "benefit committee." And indeed, some creditors, like DIP lenders, may step into a fiduciary relationship with the bankruptcy estate if they wield extraordinary control over the estate's decisionmaking. The timing is right for a rethinking: as the social enterprise ecosystem finds itself caught up in bankruptcy proceedings, creditors and debtors alike may wish to press for their vision of value. This vision for bankruptcy law is both capacious and controversial: it would allow for a wider range of values to be pursued during the plan negotiation process

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[*] Assistant Professor, University of Florida Levin College of Law. This Article has been transformed over a season of workshops and presentations, and I am deeply grateful to all the scholars, practitioners, and judges who raised challenges, threw out ideas, and took my rambling phone calls. For comments and conversations that have enriched this article, I am grateful to Lynn LoPucki, David Skeel, Lars Noah, Craig Goldblatt, Jeff Bast, Hamid Rafatjoo, Mette Kurth, John A.E. Pottow, Rob Rhee, Grace Robson, Richard Squire, Danielle Reyes, Isley Gostin, Cathy Hwang, Peter Molk, Robert Miller, Michael Ohlrogge, and workshop participants at the Wharton-Harvard Insolvency & Restructuring Conference, the National Conference of Bankruptcy Judges, and the University of Florida Levin College of Law's Faculty Scholarship Roundtable. Zach Torres ('24), Sarah Jones ('24), Jonathan Giron ('24), and Lema Hussein ('25) contributed thoughtful research, incisive comments, and diligent editing. All remaining errors are my own.

and could reshape bankruptcy practice for social enterprises.

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INTRODUCTION

The time-honored notion that businesses can "do well" and "do good" at the same time has found new verve in the Millennial and Gen Z generations.[1] The idea has travelled under various names over its long history,[2] but is commonly referred to today as corporate social responsibility ("CSR") or environmental, social, and governance metrics ("ESG").[3] We do not yet fully understand, though, whether this movement can survive the crucible of bankruptcy court. Does social enterprise end with insolvency? Is bankruptcy all about the bottom line?

In this Article, I lay the foundation for answering those questions with a resounding *no*. But the reason is complicated. That's because a petition filed under the Bankruptcy Code[4] transfers the assets of an insolvent firm into an estate. The estate is then managed and operated by a trustee, although usually the debtor company is allowed to step into the trustee's shoes — an innovative feature of American insolvency law that has been exported around the world.[5] For their part, creditors are transformed into the beneficiaries of the estate, organized into committees, and sometimes even asked to fund the case. So the same cast of characters exercises control over the estate, but in different ways, to different ends, and wearing different legal caps.

Bankruptcy's separation of ownership and control suggests that we should find some answers about the fate of social enterprise in fiduciary duty law. After all, fiduciaries are required to put others' interests above their own, so if anyone would be championing social causes in insolvency court, it would be bankruptcy fiduciaries. But the dynamics described above make

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[1] *See, e.g.*, Teresa McGlone et al., *Corporate Social Responsibility and the Millennials*, 86 J. EDUC. FOR BUS. 195, 199 (2011) (discussing millennial tendency towards employee volunteerism on corporate social responsibility efforts).

[2] *See, e.g.*, Judd F. Sneirson, *Green is Good: Sustainability, Profitability, and a New Paradigm for Corporate Governance*, 94 IOWA LAW REV. 987, 991–92 (2009) (explaining the "triple-bottom-line" approach as encompassing not only a company's traditional financial performance but also its sustainability and broader societal impact).

[3] *Id*. Of course, CSR and ESG are each controversial in their own way. The investment firm Blackrock, for example, said it would pursue ESG goals in its funds, then backed off under pressure. *See* Justin Worland, *Larry Fink Takes on ESG Backlash*, TIME (June 29, 2023), https://time.com/6291317/larry-fink-esg-climate-action/. And in red states like Florida, CSR and ESG measures have come under heavy fire. *See, e.g.*, Conor Friedersdorf, *How the Right and the Left Switched Sides on Big Business*, THE ATLANTIC (May 19, 2023), www.theatlantic.com/ideas/archive/2023/05/free-speech-corporations-desantis-disney-citizens-united/674111/.

[4] Bankruptcy Reform Act of 1978, Pub. L. No. 95-595, 92 Stat. 2549 (codified at 11 U.S.C. §§ 101 *et seq.*) [hereinafter the "Bankruptcy Code" or the "Code"].

[5] 11 U.S.C. § 1108. For a discussion of the Congressional debate, see Robert J. Berden & Bruce G. Arnold, *Displacing the Debtor in Possession*, 67 MARQ. L. REV. 457 (1984).

a muddle of fiduciary duty law, which is messy during the best of times.

Imagine a delivery company — let's call it "Green Creek" — that is dedicated to sustainability and providing jobs in its local economy. To distinguish its own brand from the brown UPS trucks and the blue Amazon trucks, Green Creek uses delivery trucks that are green, both metaphorically and literally. The green trucks cost more to purchase and maintain but have a lower environmental impact. Green Creek is a Delaware benefit corporation and has listed the environment and the local economy as specific public benefits that its board must balance alongside profit.

If Green Creek becomes insolvent, how should its directors think about their fiduciary duties? Can they keep the green trucks, or should they change over to the more profitable (and perfectly legal) brown trucks? If they decide to sell the company, can they sell to another benefit corporation or must they select the highest bidder? What if Amazon or UPS attempts a hostile takeover?

Now imagine that Green Creek tries to reorganize under chapter 11 of the Bankruptcy Code. Do its fiduciary duties change because of the bankruptcy petition? Does it matter if the board's bankruptcy strategy is an asset sale or a plan? And what happens if Green Creek realizes the only path left is to liquidate and wind up the business under chapter 7 of the Code?

Scholars are only beginning to grapple with these questions. In 2017, Professor Jonathan Brown argued that social enterprises should not lose their distinctive take on value in bankruptcy and proposed several legislative initiatives that would secure that outcome.[6] In *Bankruptcy & the Benefit Corporation*, I engaged in the first scholarly exploration of what might happen under current law when a benefit corporation files for bankruptcy.[7] In that article, I argued that the public benefit promised at formation should persist into insolvency, reorganization, and even liquidation.[8] And I raised a series of questions challenging the assumption that bankruptcy law is inhospitable to public benefit. By contrast, Professors Dana Brakman Reiser and Steven A. Dean have argued that "[b]ankruptcy is an especially fraught type of exit for social enterprises," and propose out-of-court alternatives instead.[9]

Empiricists are starting to fill in the picture too. A 2018 study by Professors K.C. Lin and Xiaobo Dong shows that firms who practice CSR

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[6] Jonathan Brown, *When Social Enterprises Fail*, 62 VILL. L. REV. 27, 28 (2017).

[7] Christopher D. Hampson, *Bankruptcy & the Benefit Corporation*, 96 AM. BANKR. L. J. 93, 98–99, 137 & n.222 (2022) (surveying the literature).

[8] *See id.* at 137 & n.222.

[9] DANA BRAKMAN REISER & STEVEN A. DEAN, SOCIAL ENTERPRISE LAW: TRUST, PUBLIC BENEFIT, AND CAPITAL MARKETS 165 (2017). Like Brown, I think that "the benefit corporation's commitment to general and specific public benefit should not vanish at the onset of financial distress." Hampson, *supra* note 7, at 99.

build up a form of social capital that makes them less likely to file for bankruptcy in financial distress and more likely to enjoy a faster recovery process.[10]

Now, in fairness, the tack of this Article may seem ill-timed to some readers. Most recently, bankruptcy judges, scholars, and practitioners have been grappling with the sharp-elbow tactics of hedge funds, distressed debt, big law, and business-friendly courts. Driven by lenders since the 1990s,[11] and more recently sponsors,[12] the most powerful players in bankruptcy cases are often willing to play what Professors Jared Ellias and Robert Stark call "bankruptcy hardball,"[13] resulting in "creditor-on-creditor violence" or what Professor Diane Lourdes Dick calls "hostile restructurings."[14] Aggressive bankruptcy strategies lead debtors' counsel to prefer filing in districts not subject to unfavorable precedent or stickler judges. The ensuing forum- or judge-shopping has produced a "race to the bottom" that Professor Lynn LoPucki (along with others) has criticized as corrupt and lawless.[15]

Yet this gamesmanship is neither the history nor the future of American bankruptcy practice. Indeed, the "credit men" of the early twentieth century, as Professor Douglas Baird introduces them in his recent monograph on bankruptcy law, long advanced a lenient approach to debtors — at least those

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[10] K.C. Lin & Xiaobo Dong, *Corporate Social Responsibility Engagement of Financially Distressed Firms and Their Bankruptcy Likelihood*, 43 ADV. IN ACCOUNTING 32, 41 (2018).

[11] *See, e.g.*, David A. Skeel Jr., *Creditors' Ball: The New New Corporate Governance in Chapter 11*, 152 U. PA. L. REV. 917, 918 (2003).

[12] *See* Vincent S.J. Buccola, *Sponsor Control: A New Paradigm for Corporate Reorganization*, 90 U. CHI. L. REV. 1 (2023).

[13] Jared A. Ellias & Robert J. Stark, *Bankruptcy Hardball*, 108 CALIF. L. REV. 745 (2020).

[14] *See, e.g.*, Douglas G. Baird, *Three Faces of Creditor-on-Creditor Aggression*, 97 AM. BANKR. L.J. 213 (2023); Diane Lourdes Dick, *Hostile Restructuring*, 96 WASH. L. REV. 1333 (2021) (discussing lender-on-lender violence). Skeel also talks about sly creditor strategies in the debt finance world, such as "trapdooring" and "uptiering," that have insolvency practitioners triple-checking the credit documents. David A. Skeel, Jr., *Bankruptcy's Identity Crisis*, at *3 (forthcoming U. PENN. L. REV.) (on file with author). For a recent examination on the breakdown in congenial negotiations in bankruptcy, *see* Diane Lourdes Dick, *Alliance Politics in Corporate Debt Restructurings*, 39 EMORY BANKR. DEV. J. 285 (2023). And for a helpful discussion and incisive criticism of loan-to-own strategies, especially via convertible DIP loans, *see* Robert W. Miller, *Loan-to-Own 2.0* (unpublished manuscript) (on file with author).

[15] *See, e.g.*, Lynn M. LoPucki, *Chapter 11's Descent into Lawlessness*, 96 AM. BANKR. L.J. 247 (2022); Adam J. Levitin, Purdue*'s Poison Pill: The Breakdown of Chapter 11's Checks and Balances*, 100 TEX. L. REV. 1079, 1099–1103 (2022). Professor LoPucki's campaign goes back over twenty years, dating back to a 1991 article on venue choice and forum shopping in chapter 11, *see* Lynn M. LoPucki & William C. Whitford, *Venue Choice and Forum Shopping in the Bankruptcy Reorganization of Large, Publicly Held Companies*, 1991 WISC. L. REV. 11, and cresting in a 2006 monograph, LYNN M. LOPUCKI, COURTING FAILURE (2006).

debtors who are "honest but unfortunate."[16] So long as the business enterprise has a credible shot at a profitable business plan, and so long as its principals are forthright and willing to keep striving, creditors are willing to negotiate second chances.

As for the nature and source of fiduciary duties in bankruptcy, one could be forgiven for thinking that it would be settled, black-letter law. Instead, the law here is undertheorized, conflicted, and muddled. Congress gave no answers in the Code itself, nor has the Department of Justice or the U.S. Trustee's Office provided any meaningful interpretive guidance. In *CFTC v. Weintraub*,[17] the Supreme Court said that the trustee has a duty to "maximize the value of the estate," but *Weintraub* was a chapter 7 liquidating case, and that maxim provides limited guidance in cases where the debtor is attempting to reorganize as a going concern. As Professor Daniel B. Bogart put it twenty-five years ago, "This law is confusing and untidy; the parlance of both state corporate governance law and trust law is used at different times by different courts, often without analysis and often without fidelity to key distinctions and concepts in the sources that are drawn upon."[18] The ensuing quarter century has not improved the outlook.

This Article provides the first comprehensive examination of fiduciary duties in bankruptcy. I attempt (as best I can) to sort out this mess and provide a clear-eyed, comprehensive vision for this area of law, one that I hope will be helpful not just for the scholarly community, but also for practitioners and judges. I conclude that the bankruptcy trustee does not have a freewheeling duty to "maximize the value of the estate." That objective should be limited to chapter 7 cases. In reorganization cases, by contrast, the trustee's duty of obedience gives rise to what we might call a "duty to facilitate a plan" or a "duty to clear runway" for the parties to negotiate a plan. Additionally, under 28 U.S.C. § 959, the trustee must follow fiduciary duties that otherwise govern the debtor outside of bankruptcy.

For their part, debtors and creditors have space to advocate for public-minded goals as part of a bankruptcy case, working (as always) within the confines of the rules. Creditors seeking to hold a nonprofit or benefit debtor to its original mission might, for example, ask the court to appoint a "benefit

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[16] DOUGLAS B. BAIRD, THE UNWRITTEN LAW OF CORPORATE REORGANIZATIONS 50–51 (2022) ("Having sympathy for the honest but unlucky debtor, in addition to being honorable and upright, was also good business."); *see also* Grogan v. Garner, 498 U.S. 279, 286–87 (1991) ("[I]n the same breath that we have invoked this 'fresh start' policy, we have been careful to explain that the Act limits the opportunity for a completely unencumbered new beginning to the 'honest but unfortunate debtor.'") (quoting Local Loan Co. v. Hunt, 292 U.S. 234, 244 (1934)).

[17] 471 U.S. 343 (1985).

[18] Daniel B. Bogart, *Liability of Directors of Chapter 11 Debtors in Possession: "Don't Look Back — Something May Be Gaining on You*, 68 AM. BANKR. L.J. 155, 185 (1994).

committee" — a novel concept that might elegantly incorporate incommensurate perspectives into bankruptcy's rough-and-tumble system.

This vision for bankruptcy law is a capacious one, more open to different understandings of value, and therefore controversial. But if we understand commercial law as a field for creativity and experimentation, then corporate character should not be destroyed in the crucible of bankruptcy court, especially when the very purpose of the bankruptcy case is a second chance.

This Article unfolds in six parts. In Part I, I explain the bankruptcy estate and how this legal mechanism generates the bankruptcy fiduciary puzzle. In Part II, I explore fiduciary duties outside bankruptcy and why their significance is underappreciated in the bankruptcy context. From there, the Article unfolds in three parts, each of which grapples with a different bankruptcy fiduciary: the Trustee (Part III), the Debtor (Part IV), and the Creditors (Part V).[19] Part VI steps back to review the structure of fiduciary duties in bankruptcy, which I suggest are multi-layered, or "stacked." I conclude with a "new old" vision for business bankruptcy.

I. WHAT DOES IT MEAN TO GO INTO BANKRUPTCY?

We begin our exploration of bankruptcy fiduciaries by interrogating the purpose of bankruptcy — and what it means that U.S. bankruptcy law

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[19] I have had to exclude at least two other important bankruptcy fiduciaries, both for space and because they are not a feature of every bankruptcy case.

First is the bankruptcy examiner, who can investigate the debtor while allowing the DIP to operate the business. 11 U.S.C. § 1104. The late Professor Christopher Frost proposed the increased use of examiners in 1992. *See* Christopher W. Frost, *Running the Asylum: Governance Problems in Bankruptcy Reorganizations*, 34 ARIZ. L. REV. 89, 138 (1992). And Frost's vision may be materializing: the Third Circuit recently required an examiner in the *FTX* bankruptcy, holding that the statute mandated an examiner upon request by the U.S. Trustee. *In re* FTX Trading Ltd., No. 23-2297, 2024 WL 204456 (3d Cir. Jan. 19, 2024).

Second is the consumer privacy ombudsman or "ombud," whom the U.S. Trustee appoints when a proposed sale under section 363 would include the transfer of personally identifiable information ("PII") to a third party. *See* 11 U.S.C. §§ 332, 363(b)(1). For a comprehensive discussion of the bankruptcy consumer privacy ombudsman that grapples with both the bankruptcy and the privacy literature, see Christopher G. Bradley, *Privacy for Sale: The Law of Transactions in Consumers' Private Data* (forthcoming YALE J. REG. 2024) (manuscript on file with author); *see also* Laura M. Coordes, *Unmasking the Consumer Privacy Ombudsman*, 82 MONT. L. REV. 17 (2021); Diane Lourdes Dick, *The Bankruptcy Playbook for Dealing with Valuable Data Assets*, 42 BANKR. L. LETTER (Jan. 2022); Kayla Siam, *Coming to a Retailer Near You: Consumer Privacy Protection in Retail Bankruptcies*, 33 EMORY BANKR. DEV. J. 487 (2017); Stacy-Ann Elvy, *Commodifying Consumer Data in the Era of the Internet of Things*, 426 B.C. L. REV. 423, 475–83 (2018); Edward J. Janger, *Muddy Property: Generating and Protecting Information Privacy Norms in Bankruptcy*, 44 WM. & MARY L. REV. 1801, 1873–77 (2003).

operates through the creation of an estate.[20] For as Justice Frankfurter wrote eighty years ago, "to say that a man is a fiduciary only begins analysis …. To whom is he a fiduciary?"[21] In the bankruptcy context, the answer to the question "to whom" is the estate and its beneficiaries.[22]

A. Of Metaphors & Technicalities

Most people cannot help but use metaphors for the bankruptcy process. We talk about an individual or business enterprise "going into" bankruptcy and then "emerging" — as if the company had gone into a tunnel.[23] I am guilty of this habit at times, referring to "navigating" the bankruptcy process, as if the debtor were an embattled ship crashing through stormy waters.[24]

Such metaphors can be misleading. Technically, the filing of a petition in bankruptcy creates an estate, rather like death.[25] Into the estate goes most of the debtor's property.[26] And upon the commencement of the case, an automatic stay goes into effect, preventing creditors from attempting to collect while the case is pending and shielding the estate from unilateral action by its new beneficiaries.[27]

The connection to death is both metaphorical and institutional. Until Congress passed a permanent bankruptcy statute, probate courts in many jurisdictions supervised both kinds of estates. Even today, if one strolls by the Suffolk County Courthouse at 3 Pemberton Square in Boston, Massachusetts, one can see a plaque reflecting the connection:

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[20] I will use the singular *estate*, *trustee*, *debtor*, and so on, even though large business enterprises today operate through a family of related corporate entities, and their bankruptcy filings are sets of cases that are procedurally consolidated. *See, e.g.*, Raymond T. Nimmer & Richard B. Feinberg, *Chapter 11 Business Governance: Fiduciary Duties, Business Judgment, Trustees and Exclusivity*, 6 BANKR. DEV. J. 1, 42 (1989).

[21] *S.E.C. v. Chenery Corp.*, 318 U.S. 80, 85–86 (1943).

[22] *See Pepper v. Litton*, 308 U.S. 295, 306–07 (1939) ("A director is a fiduciary. So is a dominant or controlling stockholder or group of stockholders. Their powers are powers in trust. … While normally that fiduciary obligation is enforceable directly by the corporation, or through a stockholder's derivative action, it is, in the event of bankruptcy of the corporation, enforceable by the trustee. For that standard of fiduciary obligation is designed for the protection of the *entire community of interests* in the corporation — creditors as well as stockholders) (emphasis added) (internal citations omitted).

[23] *See, e.g.*, Dietrich Knauth, *Revlon Emerges from Bankruptcy After Lender Takeover*, Reuters (May 2, 2023), www.reuters.com/business/retail-consumer/revlon-emerges-bankruptcy-after-lender-takeover-2023-05-02/.

[24] *See* Hampson, *supra* note 7, at 127, 134.

[25] 11 U.S.C. § 541(a).

[26] *Id.* § 541(a)(1)–(6). Section 541(b) of the Bankruptcy Code also contains exclusions from the estate, which serve to define more crisply the boundaries of the debtor's property. *See id.* § 541(b).

[27] *Id.* § 362.

Photograph taken by author in 2022.

Even as assets are moved from the debtor into an estate, liabilities are reinvented as claims against the estate, and the claimants become the estate's beneficiaries. Anyone with a claim (defined expansively[28]) must file a "proof of claim" against the estate, and those claims will be categorized as secured or unsecured and as receiving priority or nonpriority ("general") treatment.[29]

The size and timing of distributions to claimants depends on the economic health of the estate and whether the bankruptcy is a reorganization case or a liquidation case. But as a general rule, secured claimants receive the economic benefit of their liens; priority claimants receive distributions before other creditors; and general unsecured claimants receive *pro rata* or proportional distributions from whatever is left.[30] When the case is over, the property of the estate is either gone (liquidated during the course of the case or conveyed to a liquidation trust) or it re-vests in the debtor.[31]

Nothing about this approach is written in stone. As central as the concept of the estate is to modern U.S. bankruptcy law, a legal architect could design an insolvency system without using the concept of an estate at all. Many of the key provisions — like the automatic stay — would use "property of the

[28] *See id.* § 101(5).
[29] *Id.* §§ 506 & 507.
[30] *Id.* §§ 506 & 507.
[31] *See, e.g.*, *id.* § 1141(b).

debtor" as the key concept instead of "property of the estate."[32] If the debtor cannot be trusted to manage itself, the bankruptcy court could simply appoint a receiver or a guardian to manage and operate the debtor's affairs. This is how insolvency proceedings operate under Shari'a law,[33] it is how equity receiverships operate under state law,[34] and it is how bank receiverships operate under Title 12.[35]

By creating an estate, the Bankruptcy Code goes a step farther than replacing management. It implements an artificial, costless transfer of the debtor's property to a new structure.

B. Of Estates & Enterprises

It is equally misleading to imagine the bankruptcy estate as a passive collection of assets, as if someone wheeled a freezer into the courtroom until everyone could figure out what to do with the contents. Even for businesses that are on the verge of liquidation, the estate is an enterprise that continues to operate during the bankruptcy case — the closest existing thing to the business the day before it filed for bankruptcy. At the most technical level, there are at least three ways in which the Bankruptcy Code narrows the gap between the estate and the enterprise that preceded it.

First, *property* is an expansive and fluctuating category in the Bankruptcy

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[32] Most of section 362 refers to "property of the estate," but subsection 5 applies the automatic stay to "any act to create, perfect, or enforce against property of the debtor any lien to the extent that such lien secures a claim that arose before the commencement of the case under this title." 11 U.S.C. § 362(a)(5). In bank liquidations, by comparison, the FDIC can simply ask for a stay of all proceedings to which the bank is a party. 12 U.S.C. § 1821(d)(12).

[33] Islamic law does not contain noncharitable trusts, so Islamic insolvency proceedings are not structured with a trustee. Instead, the court appoints a receiver (*rajul thiqah*) to manage and operate the debtor's property. A distraint order, the converse of the automatic stay, enjoins the debtor from attempting to manage its property. *See* Abed Awad & Robert E. Michael, *Iflas and Chapter 11: Classical Islamic Law and Modern Bankruptcy*, 44 INT'L LAW. 975, 989 & n.102 (2010).

[34] *See, e.g.*, Stephen J. Lubben, *Railroad Receiverships and Modern Bankruptcy Theory*, 89 CORNELL L. REV. 1420, 1441–42 (2004).

[35] Banks are unable to file for bankruptcy under the Code itself. *See* 11 U.S.C. § 109; *see also* Michale I. Sovern, *Section 4 of the Bankruptcy Act: the Excluded Corporations*, 42 MINN. L. REV. 171 (1957). Instead, when banks face insolvency, the FDIC steps in as a conservator or receiver. *See* 12 U.S.C. § 1821(c)(2)(A); David A. Skeel, Jr., *Law and Finance of Bank and Insurance Insolvency Regulation*, 76 TEX. L. REV. 723, 729–31 (1998). Under those provisions, the receiver is successor to the bank's rights and can operate the bank directly. *See* 12 U.S.C. § 1821(c)(13)(B); *id.* (d)(2)(A) (providing that the FDIC is successor to "all rights, titles, powers, and privileges of the insured depository institution)) and (B) (providing that the FDIC may operate the institution). The FDIC has promulgated regulations governing how the FDIC acts as receiver. *See id.* § 1821(d)(1).

Code. The estate includes "all legal or equitable interests of the debtor in property,"[36] and courts have interpreted that phrase to encompass everything from intellectual property and causes of action to licenses and domain names.[37] And the property of the estate can expand or shrink: it captures proceeds and profits;[38] and property of the estate can be sold or abandoned.[39]

Second, the estate encompasses *contracts* as well as property. The Bankruptcy Code makes unenforceable any contractual terms that would make the act of filing for bankruptcy an event of default,[40] and gives the estate the benefit of valuable contracts, while enabling it to escape detrimental contracts.[41]

Third, the estate can be "reshaped" over the course of the bankruptcy case.[42] State law allows insolvent businesses or their creditors to unwind preferential payments and transactions that are fraudulent or unreasonably unfair to the business.[43] The Bankruptcy Code preserves those state causes of action for the estate and adds federal causes of action to boot.[44] Proceeds from those causes of action, if successful, become property of the estate.

Thus, even though business enterprises do not "go into" bankruptcy as a formal matter, the technical legal reality is much more complex.

This multifaceted structure has generated many a thorny legal puzzle. In *Weintraub*, the Supreme Court had to decide who had authority to waive the attorney-client privilege for pre-bankruptcy communications: the debtor or the trustee in bankruptcy. The client at the time of the communications, of course, was the debtor. But the debtor had since filed for bankruptcy, its property had passed into the estate, and a trustee had been appointed to manage that estate. The Supreme Court analogized the bankruptcy filing to

[36] 11 U.S.C. § 541(a)(1).

[37] *See, e.g.*, Kunkel v. Jasin, 420 F. App'x 198, 199 (3rd. Cir. 2011) (holding that debtor's architectural designs were property of the estate); Putzier v. Ace Hardware Corp., 50 F. Supp. 964, 982 (N.D. Ill. 2014) (holding that debtor's fraud claim was property of the estate); *In re* Fugazy Exp., Inc., 124 B.R. 426, 430 (S.D.N.Y. 1991) (holding that debtor's FCC license was property of the estate); *In re* Luby, 438 B.R. 817, 829–30 (holding that debtor's domain names were property of the estate).

[38] 11 U.S.C. § 541(a)(6)–(7).

[39] *Id.* §§ 363, 554; Stanley v. Sherwin Williams Co., 156 B.R. 25, 26 (W.D. Va. 1993) (highlighting that specific procedures for abandonment must be followed or property remains part of the estate).

[40] 11 U.S.C. §§ 365(b)(2)(A) & 365(e)(1)(A).

[41] *Id.* § 365. "Indeed, it is the duty as well as the right of a trustee or debtor in possession to seek the court's approval for rejection of a contract as executory when such contract is burdensome to the debtor estate." *See* COLLIER ON BANKRUPTCY, 15th Ed., Vol. 2, § 365.03.

[42] ELIZABETH WARREN ET AL., THE LAW OF DEBTORS AND CREDITORS: TEXT, CASES, AND PROBLEMS 435 (8th ed. 2021).

[43] *See, e.g.*, FLA. STAT. § 726.105.

[44] 11 U.S.C. §§ 545, 546, 547 and 548.

the passing of control of a corporation to new management, and on that basis decided that the entity exercising control over the estate should be able to waive the attorney-client privilege — in that case, the trustee.[45]

If debtors simply "entered" bankruptcy, the puzzle of bankruptcy fiduciaries would be vastly simplified. Directors and officers of bankrupt corporations would owe the same fiduciary duties in bankruptcy as they did before bankruptcy, whether duties of care, loyalty, obedience, or balancing, and they would owe them to the same people. But because a filing in bankruptcy creates an estate, it is not immediately obvious who owes fiduciary duties to the estate and its beneficiaries and (if so) what those fiduciary duties are.[46]

C. Of Creditors and Beneficiaries

A bankruptcy filing works some surprising changes upon the creditors as well, transforming them from a motley aggregate into a creditor body: the beneficiaries of the estate. A debtor on the eve of bankruptcy typically owes various types of debts. Some of those debts are financial and can be calculated precisely or have been reduced to judgment, but others are contingent, unmatured, or hotly contested. The Bankruptcy Code sweeps all of these creditors into bankruptcy court by defining "claim" as a

> right to payment, whether or not such right is reduced to judgment, liquidated, unliqudiated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured.[47]

To receive a distribution from the bankruptcy estate, creditors must file a "proof of claim."[48]

But the creditors' claimed position in line is not something bankruptcy attorneys take for granted. Any party in interest can object to a proof of claim,

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[45] 471 U.S. 343, 351-52 (1985) ("In light of the lack of direct guidance from the Code, we turn to consider the roles played by the various actors of a corporation in bankruptcy to determine which is most analogous to the role played by the management of a solvent corporation. Because the attorney-client privilege is controlled, outside of bankruptcy, by a corporation's management, the actor whose duties most closely resemble those of management should control the privilege in bankruptcy, unless such a result interferes with policies underlying the bankruptcy laws."); *see also* Digital Media Solutions, LLC v. South University of Ohio, LLC, 59 F.4th 772, 780 (6th Cir. 2023) ("The receiver stood in the shoes of the corporate debtor, taking possession of all its property and becoming its manager.").

[46] *See* SEC v. Chenery Corp., 318 U.S. 80, 85–86 (1943); *see also* Stephen J. Lubben, *Taking Corporate Bankruptcy Fiduciary Duties Seriously*, at 15 (forthcoming J. CORP. L. 2023) (manuscript on file with author).

[47] 11 U.S.C. § 101(5); Ohio v. Kovacs, 469 U.S. 274 (1985).

[48] 11 U.S.C. §§ 501, 502.

and raging fights sometimes break out — especially when a creditor incorrectly states that its debt is secured.[49] But a party in interest could also object to the amount of the claim, its priority status, or even whether it is owed at all.[50]

But that's not all. The "reshaping" of the estate described above not only reworks the property of the estate but also reorders the claims against it. A creditor who received a preferential or fraudulent payment and repays it to the estate receives, in exchange, a claim against the estate: their proper place in line.[51] A contract counterparty left behind by a reorganizing or liquidating debtor receives a claim as of the date of the petition.[52]

Like any estate, the bankruptcy estate has "claimed beneficiaries" and "true beneficiaries," but sorting out which is which, and clarifying the size and nature of each claim against the estate, is a drawn-out, sometimes hotly litigated process that pits the estate's managers against those who would seek to benefit from the estate.

D. The Purpose of Bankruptcy

What is all this for? To what end does federal bankruptcy law allow debtors (or, under some circumstances, their creditors) to file a petition in bankruptcy and transfer their assets into an estate? At the most theoretical level, bankruptcy scholars and practitioners alike recite the value of providing a "fresh start to the honest but unfortunate debtor,"[53] preserving "go-forward value" in profitable businesses overburdened by debt, and (bankruptcy at its most bleak) an orderly liquidation process. As a law partner once told me over dinner in a Manhattan restaurant during my first months as an insolvency attorney, "every bankruptcy has a story."

These goals map onto the different chapters under which debtors may file in the Bankruptcy Code. Chapter 7 cases are focused on orderly liquidation and, for individuals, a "fresh start." In such cases, the trustee must "collect and reduce to money the property of the estate" and close the estate "as expeditiously as is compatible with the best interests of parties in interest."[54] The other chapters — 9, 11, 12, and 13 — all attempt to preserve go-forward

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[49] 11 U.S.C. § 502(a); *see also* Fin. Oversight & Mgmt. Bd. for P.R. v. U.S. Bank Nat'l Assoc., 649 B.R. 381 (D.P.R. 2023) (analyzing whether Puerto Rico municipal bondholders held secured claims).

[50] The Bankruptcy Code itself modifies certain kinds of claims, such as the Code's flat disallowance of unmatured interest, which (with some exceptions) stops the interest clock on financial debt as of the date of the petition. 11 U.S.C. §§ 502(b)(1), 506.

[51] *Id.* § 502(h).

[52] *Id.* §§ 365(g); 502(g).

[53] *See supra* note 16.

[54] 11 U.S.C. § 704(a)(1).

value and deliver a fresh start through a "repayment" or "reorganization" plan. Crucially, bankruptcy plans require that the estate be more valuable as a "going concern" than if it were to liquidate instead, and the Code sets complex rules governing which groups of creditors should receive that additional value and in what order.[55]

As above, our metaphors for the final stages of this process often fail to reflect the legal concepts involved. Insolvency professionals speak of a business "emerging" from bankruptcy. Actually, it's more like a transfer: the property of the estate re-vests in the debtor either upon confirmation or after payments have been completed.[56]

Anyone who has studied (or litigated) corporate governance knows that it is complex during the best of times. Bankruptcy extends that complexity along multiple dimensions: it is not the best of times, and the entire U.S. insolvency mechanism operates through the creation of a new entity, one that walks alongside the debtor during the bankruptcy case, bears its burdens for a time, and then vanishes when the case closes. We turn now to one of the most intractable puzzles generated by this dynamic: bankruptcy fiduciaries.

II. FIDUCIARIES IN A MAZE OF RULES

Bankruptcy fiduciaries have a profound impact on the trajectory of bankruptcy cases, but their obligations are poorly understood. This lack of clarity is partly due to the constraining maze of bankruptcy rules that govern and guide bankruptcy fiduciaries. At root, though, the bankruptcy rules do not definitively settle the question of the fiduciary duties owed to the estate, and as social enterprises continue to foot or fall into bankruptcy courts, the courts will need to figure out whether the trajectory of their cases is any different. As the reader will see, I argue that the bankruptcy cases of social enterprises *should* work a little differently. To reach that result, I begin with an overview of fiduciary duty law; explain why fairness, efficiency, and formation concerns point toward that result; and show why it matters in bankruptcy court.

A. The Law of Fiduciary Duties

Both inside and outside bankruptcy, fiduciary duties matter tremendously to decisionmaking. In corporate law, fiduciary duties blanket the landscape

[55] For example, in chapter 11, the Code requires that each claimholder receive equal or greater value under the plan than they would in a chapter 7 liquidation. 11 U.S.C. § 1129(a)(7). That rule incorporates the chapter 7 priority structure, located in sections 726 and 507 of the Code.

[56] *See* 11 U.S.C. § 1227(b), 1327(b).

of corporate governance, including decisions whether to slash business lines, take on additional debt, or file for bankruptcy protection.

Arising out of agency law, fiduciary duties are obligations owed by an agent to a principal to put the principal's interests over their own.[57] That basic principle has taken different shapes in different areas of law.

First, in trusts and estates, trustees have fiduciary duties to the estate created by the trust instrument,[58] as well as fiduciary duties created by common law, the most important being prudence, loyalty, impartiality, and delegation.[59] The standard of conduct is demanding; as Judge Cardozo opined, the standard for trustees is "the punctilio of an honor the most sensitive."[60]

The duty of prudence tasks the trustee with acting as a "prudent person," requiring "reasonable care, skill, and caution."[61] For investment trusts, for example, the trustee must both preserve the trust principal and generate income.[62] Unlike in tort law, though, if the trustee possesses more skill "than that of a person of ordinary prudence, the trustee has a duty to use such

[57] *See, e.g.*, RESTATEMENT (THIRD) OF AGENCY § 8.01.

[58] *See* DANAYA C. WRIGHT ET AL., WILLS, TRUSTS, AND ESTATES: AN INTEGRATED APPROACH 361 (2021) (noting that trustees "must comply with whatever administrative provisions are established by the trust instrument and state trust laws") (citing Marsman v. Nasca, 573 N.E.2d 1025 (Mass. App. Ct. 1991)).

[59] The Second Restatement, expanding on the duties in the First, specified sixteen trustee fiduciary duties. *See* RESTATEMENT (SECOND) OF TRUSTS, §§ 169–185; RESTATEMENT (FIRST) OF TRUSTS, §§ 169–185. By contrast, the Third Restatement separates the discussion of trustee fiduciary duties into general principles and specific duties. *See* RESTATEMENT (THIRD) OF TRUSTS, § 70 cmt. a ("[A] power expressly conferred by the trust instrument, or by statute, is subject to the fundamental duties of prudence, loyalty, and impartiality, to a duty to adhere to the terms of the trust, and to the other fiduciary duties of trusteeship, all as stated, qualified, and applied … elsewhere in this Restatement.").

[60] Meinhard v. Salmon, 164 N.E. 545, 546 (N.Y. 1928) ("Many forms of conduct permissible in a workaday world for those acting at arm's length, are forbidden to those bound by fiduciary ties. A trustee is held to something stricter than the morals of the market place. Not honesty alone, but the punctilio of an honor the most sensitive, is then the standard of behavior. As to this there has developed a tradition that is unbending and inveterate.").

[61] RESTATEMENT (THIRD) OF TRUSTS § 77(1)–(2); *see also* MELANIE B. LESLIE & STEWART E. STERK, TRUSTS AND ESTATES 154–161 (4th ed. 2021) (discussing the difference between the traditional and modern approach to the trustee's duty of care); JEFFREY N. PENNELL & ALAN NEWMAN, QUICK REVIEW OF WILLS, TRUSTS, AND ESTATES 547–48, 559 (6th ed. 2019) (discussing the duty of prudence).

[62] LESLIE & STERK, *supra* note 61, at 154–56. This objective, of course, does not entail unnecessarily risking the trust principal to generate income. *Id.* The modern portfolio theory, adopted in the early 1990s, reformed the prudent investor rule. *Id.* at 156 (citing RESTATEMENT (THIRD) OF TRUSTS, § 77). The modern prudent investor rule applies to the "trust portfolio as a whole," not only to individual investments. LESLIE & STERK, *supra* note 61, at 156. An individually speculative investment could avoid liability as long as the trust portfolio is adequately diversified. LESLIE & STERK, *supra* note 61, at 156–57.

facilities or skill."[63]

The duty of loyalty provides that a "trustee has a duty to administer the trust solely in the interest of the beneficiaries, or solely in furtherance of its charitable purpose."[64] The duty prohibits self-dealing and requires the trustee to deal "fairly and to communicate to the beneficiary all material facts the trustee knows or should know."[65]

The duty of impartiality charges the trustee to treat multiple beneficiaries fairly and equally.[66] This does not imply treating beneficiaries "equally," but instead "to seek to ascertain and to give effect to the rights and priorities of the various beneficiaries or purposes as expressed or implied by the terms of the trust."[67]

The duty of delegation governs when a trustee may delegate tasks to others.[68] The trustee must exercise its discretion prudently when it selects delegates and supervises them.[69]

Second, in corporate governance, like in trusts and estates, fiduciary duties arise out of the separation of ownership and control.[70] Companies owe fiduciary duties to their shareholders; directors and officers of the company owe them to the company; and controlling shareholders owe them to minority shareholders.[71] Given this reticulated web of duties, legal actions to enforce fiduciary duties are brought both directly and derivatively, both as individual enforcement actions and as class actions.[72]

The content of fiduciary duties — or the standard of conduct — depends on the nature of the business organization involved:

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[63] RESTATEMENT (THIRD) OF TRUSTS § 77(3).

[64] *Id.* § 78(1); *see also* LESLIE & STERK, *supra* note 61, at 149–54 (discussing the prohibition on self-dealing and various exemptions); PENNELL & NEWMAN, *supra* note 61, at 548–55 (describing the duty of loyalty as "[a]rguably, the highest duty the common law imposes").

[65] RESTATEMENT (THIRD) OF TRUSTS, § 78(1)–(2).

[66] *Id.* § 79.

[67] *Id.* § 79 cmt. b. This duty is an extension of the duty of loyalty, and applies only when a trust has "two or more beneficiaries or purposes." *Id.* § 79 cmt. a.

[68] *Id.* § 80.

[69] *Id.* § 80(1)–(2); *see also* PENNELL & NEWMAN, *supra* note 61, at 559 ("[A] fiduciary must use care and prudence in exercising the discretion to delegate, both in selecting delegates and in supervising them.").

[70] *In re* Pattern Energy Grp. Inc., 2021 Del. Ch. LEXIS 90, at *96–97 (Del. Ch. 2021).

[71] *See, e.g.*, Hampson, *supra* note 7, at 104.

[72] Direct actions are brought by someone owed a fiduciary duty who claims that the defendant (whether the corporation or its directors and officers) breached that duty. Derivative actions are brought on behalf of the corporation itself; to bring them, the nominal plaintiff must first ask the directors to bring the claim or show why it would have been a waste of time to do so (called "demand futility"). *See, e.g.*, United Food and Comm. Workers Union and Participating Food Indus. Emps. Tri-State Pension Fund v. Zuckerberg, 262 A.3d 1034, 1058 (Del. 2021) (adopting universal three-part test for demand futility).

To start, all corporations are owed two standard fiduciary duties, the duty of care and the duty of loyalty. The duty of care requires directors to make reasonable, well-informed decisions and to exercise oversight of the corporation by investigating credible concerns or safety hazards.[73] The duty of loyalty requires directors to act disinterestedly, to put the corporation's interests above their own, and to forego remunerative opportunities that would compete with the corporation.[74]

But this is only the standard package. Some firms operate under what we might call "enhanced" fiduciary duties. Nonprofit corporations and benefit corporations are each owed additional fiduciary duties. Directors of nonprofit corporations owe a duty of obedience to the charitable purpose set forth in their articles of incorporation.[75] Similarly, benefit corporations are required to have a specific or general public benefit set forth in their articles of incorporation. Directors of benefit corporations must consider that public benefit alongside the profit motive in their decisionmaking, what I will refer to here as a duty of balancing.[76]

Other firms, by contrast, expressly waive fiduciary duties. Delaware law, for example, allows LLCs and LPs to waive the fiduciary duties that their members, officers, and directors would otherwise owe.[77]

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[73] *See In re* Caremark Int'l Inc. Deriv. Litig., 698 A.2d 959 (Del. Ch. 1996); *see also* Hampson, *supra* note 7, at 105 (quoting Marchand v. Barnhill, 212 A.3d 805 (Del. 2019)). The precise scope of the *Caremark* duty, sometimes called a "duty of oversight" continues to be sketched out in Delaware and other states. The Delaware Court of Chancery recently clarified that officers also owe *Caremark* duties. *See* In re McDonald's Corp. S'holder Deriv. Litig., 291 A.3d 652 (Del. Ch. 2023); In re McDonald's Corp. S'holder Deriv. Litig., 2023 Del. Ch. LEXIS 255 (Del. Ch. Jan. 26, 2023).

[74] *See* Guth v. Loft, Inc., 23 Del. Ch. 255, 270–71 (1939).

[75] *See, e.g.*, Manhattan Eye, Ear & Throat Hosp. v. Spitzer, 715 N.Y.S.2d 575, 593 (N.Y. Sup. Ct. 1999); Alan R. Palmiter, *Duty of Obedience: The Forgotten Duty*, 55 N.Y.L. SCH. L. REV. 457, 460 (2011); Peggy Sasso, *Searching for Trust in the Not-for-Profit Boardroom: Looking Beyond the Duty of Obedience to Ensure Accountability*, 50 UCLA L. REV. 1485, 1529 (2003); BRAKMAN REISER & DEAN, *supra* note 9, at 174 n.25; Linda Sugin, *Resisting the Corporatization of Nonprofit Governance: Transforming Obedience into* Fidelity, 76 FORDHAM L. REV. 893, 897–905 (2007). As Professor Peter Molk has observed in a study of where nonprofits incorporate, the content of nonprofit fiduciary duties turns on the state of incorporation. Peter Molk, *Where Nonprofits Incorporate and Why It Matters*, 108 IOWA L. REV. 1781, 1788, 1794–95 (2023).

[76] *See, e.g.*, Hampson, *supra* note 7, at 112–13 & nn.109–113. The benefit corporation form has provoked some controversy. Professor Ofer Eldar criticizes the benefit corporation model and proposes a social enterprise legal form that would come with the fiduciary duty to maintain a social enterprise certification. Ofer Eldar, *Designing Business Forms to Pursue Social Goals*, 106 VA. L. REV. 937, 964–68, 994 (2020); *see also* Ofer Eldar, *The Role of Social Enterprise and Hybrid Organizations*, 2017 COLUM. BUS. L. REV. 92 (2017).

[77] *See, e.g.*, Peter Molk, *How Do LLC Owners Contract Around Default Statutory Protections?*, 42 J. CORP. L. 503 (2017) (describing the trend, analyzing the operating

The biggest difference between the fiduciary duties in trusts and estates and fiduciary duties in corporate governance is not the standard of conduct but the standard of review. Courts take an active role in supervising court-appointed trustees.[78] By contrast, courts hesitate to substitute their judgment for the business judgment of corporate executives.[79] Instead, courts regulate the intensity of judicial scrutiny through standards of review.[80] Under the business judgment rule (the default), courts will not disturb corporate decisionmaking that is adequately informed and disinterested. But when the board is not well informed or when members have a personal interest in the transaction, courts will review the decision for "entire fairness," a more searching form of judicial scrutiny.[81] Courts also use an intermediate standard of review in situations where the board is likely to be conflicted, such as a hostile takeover (*Unocal*[82]) or a sale of the company (*Revlon*[83])—something like heightened scrutiny. Directors may "cleanse" a transaction by obtaining the blessing of a "fully informed, uncoerced vote of the disinterested stockholders."[84]

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agreements of 283 privately owned LLCs, and suggesting that founders use such waivers "more often for opportunism and not for efficiency").

[78] *See, e.g.*, John T. Roache, Note, *The Fiduciary Obligations of a Debtor in Possession*, 1993 U. ILL. L. REV. 133, 165–67 (1993) (arguing that the higher, trustee standard should apply); Nancy B. Rapoport & C.R. Boyles, Jr., *Has the DIP's Attorney Become the Ultimate Creditors' Lawyer in Bankruptcy Reorganization Proceedings?*, 5 AM. BANKR. INST. L. REV. 47, 56 (1997) (arguing that the trustee standard of care is "more stringent" but "in practice, these two different standards are actually applied as if they were the same standard, and they impose similar duties on the DIP"); Lubben, *supra* note 46, at 29 (noting that, under a trust theory, "obvious violation of the board's duties may well lead to a more probing review of the DIP's actions, not unlike the situations where the 'entire fairness' standard is invoked under state corporate law").

[79] Brehm v. Eisner, 746 A.2d 244, 264 (Del. 2000) ("As for the plaintiffs' contention that the directors failed to exercise 'substantive due care,' we should note that such a concept is foreign to the business judgment rule. Courts do not measure, weigh or quantify directors' judgments."). For nonprofits, the attorneys general can typically sue to enforce the charter, though given the enforcement priorities of state AGs, this tactic is rarely used. *See, e.g.*, AG Racine Sues Failed Nonprofit Related to U.S. Pavilion at World's Fair for Improperly Paying Founders More than $360K in Charitable Funds (Jun. 8, 2021), https://oag.dc.gov/release/ag-racine-sues-failed-nonprofit-related-us.

[80] *See* Lyman Johnson, *The Three Fiduciaries of Delaware Corporate law — and Eisenberg's Error*, *in* FIDUCIARY OBLIGATIONS IN BUSINESS (Arthur B. Laby & Jacob Hale Russell eds., 2021)

[81] *See, e.g.*, Firefighters' Pension Sys. of City of Kansas City, Missouri Tr. v. Presidio, Inc., 251 A.3d 212 (Del. Ch. 2021) (citing *In re* Trados Inc. S'holder Litig. (Trados II), 73 A.3d 17, 44 (Del. Ch. 2013)).

[82] Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 954–55 (Del. 1985).

[83] Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 181 (Del. 1986).

[84] *Corwin v. KKR Financial Holdings LLC*, 125 A.3d 304 (Del. 2015). If the

Of course, fiduciary duties are not the only way to shape corporate decisionmaking. The obligation to follow the law and the concomitant threat of government regulation or investigation can shape corporate behavior too.[85] Corporate decisionmaking can also be shaped by incentives, such as compensation in the form of stock options.[86] Indeed, the formation of corporate culture may matter as much as (or even more than) duties or incentives.[87] As the old saying goes, personnel is policy.

Even still, fiduciary duties are the most omnipresent way to shape corporate decisionmaking. They are the bedrock of corporate governance theory. And because they stem from agency law, they allow for more widely variegated corporate values to permeate the marketplace. Fiduciary duties thus stand at the front line of shaping corporate behavior, long before societal consensus develops in ways that can shape regulatory law.

Scholars who have studied the etiology and scope of fiduciary duties justify them on various grounds.

First, fairness. Fiduciary duties ensure that when principal-agent relationships are formed, expected but unstated terms are part of the deal. This is particularly important when parties possess disproportionate information or bargaining power. As Professor Robert Rhee has recently theorized, fiduciary relationships can arise not only in the traditional principal-agent relationship, but also when "systemic and structural" power in any relationship "negates an initial strong presumption of equal footing" and is "exerted against a critical interest."[88]

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shareholders stamp a transaction with their approval, courts will deem the transaction to have complied with the duty of care. *Id.* at 312–14; *see also* Flood v. Synutra Int'l, Inc., 195 A.3d 754, 763 (Del. 2018); Kahn v. M & F Worldwide Corp., 88 A.3d 635, 644 (Del. 2014).

[85] Rosenbloom v. Pyott, 765 F.3d 1137, 1149 (9th Cir. 2014) ("[A] transaction may be so egregious on its face that board approval cannot meet the test of business judgment … These rare cases include those in which a board decides to undertake illegal activity.").

[86] Dan Cable & Freek Vermeulen, *Compensation Packages That Actually Drive Performance*, https://hbr.org/2021/01/compensation-packages-that-actually-drive-performance (Aug. 19, 2023) (discussing stock options as a short-term corporate compensation incentive).

[87] *See, e.g.*, Margaret M. Blair & Lynn A. Stout, *Trust, Trustworthiness, and the Behavioral Foundations of Corporate Law*, 149 U. PA. L. REV. 1735, 1794–96 (2001) (arguing that "fiduciary duty law works through framing, not shaming"). Indeed, Professor Paul Weitzel has recently argued that fiduciary duties can create unintended moral consequences: by signaling to officers and directors that they are acting on behalf of someone else, fiduciary duties can create a moral license for a decisionmaker to make immoral actions that they could not defend from their personal morality. *See* Paul Weitzel, *The Case Against Officer Fiduciary Duties*, at *2 (forthcoming NEB. L. REV. 2024), https://papers.ssrn.com/abstract=3783640.

[88] Robert J. Rhee, *A Liberal Theory of Fiduciary Law*, 25 U. PENN. J. BUS. L. 451, 452 (2023). For Rhee, this power-based analysis is both descriptively accurate and normatively desirable. *See id.* at 491–92.

Next, efficiency. Fiduciary duties fit snugly into the vast literature on incomplete contracts.[89] By implying fiduciary duties into principal-agent relationships, the law saves transaction costs by imposing commonly accepted terms. And even where such terms are nondisclaimable, such as in a publicly traded corporation, the law's standardization of key contractual terms underlying corporate ownership promotes efficient markets.

Lastly, formation. Fiduciary duty law encourages the development of sound habits and formative legal practices in numerous ways. It encourages the training and development of large numbers of fiduciaries in society — who, over time, become better at undertaking this salutary role. And it enables people to express themselves and build out their values in the world, through contracts and corporations that allow like-minded people to work on shared enterprises.

B. A (Relatively) Neglected Area of Bankruptcy Theory

While there is a sustained literature on fiduciary duties in corporate governance and in trusts and estates, the fiduciary duties owed to the bankruptcy estate is a muddle. This is not for lack of effort from bankruptcy luminaries over the course of at least three decades. Between 1993 and 2023, scholars such as Harvey R. Miller, Lynn LoPucki, William Whitford, Nancy Rapoport, A.E. Pottow, and Stephen J. Lubben have set forth descriptive and normative theories of fiduciary duties in bankruptcy.[90] Even so, these scholars admit that the courts have not reached anywhere near a consensus on how fiduciary duties work in bankruptcy.

Time may heal all wounds, but it does not clear up all legal doctrine. This is, in part, because the structure of bankruptcy cases makes fiduciary duties difficult to litigate. First, any fiduciary claims that could have been brought derivatively outside of bankruptcy become property of the estate and therefore can only be brought by the trustee or debtor in possession — unless

[89] *See, e.g.*, Robert E. Scott & George G. Triantis, *Incomplete Contracts and the Theory of Contract Design*, 56 CASE WEST. RESERVE L. REV. 187 (2005).

[90] Harvey R. Miller, *Corporate Governance in Chapter 11: the Fiduciary Relationship Between Directors and Stockholders of Solvent and Insolvent Corporations*, 23 SETON HALL L. REV. 1467 (1993); Rapoport & Boyles, *supra* note 78; John A.E. Pottow, *Fiduciary Principles in Bankruptcy and Insolvency*, *in* THE OXFORD HANDBOOK OF FIDUCIARY LAW 205 (Evan J. Criddle et al. eds. 2019); Lubben, *supra* note 46. In 1993, Professors Lynn LoPucki and Whitford published a sizeable empirical study of forty-three large, public companies, interviewing their management and unveiling a complex portrait of how managers perceived their scope and direction of fiduciary duty. *See* Lynn M. LoPucki & William C. Whitford, *Corporate Governance in the Bankruptcy Reorganization of Large, Publicly Held Companies*, 141 U. PA. L. REV. 669, 750–51 (1993) (describing significant limitations on managerial power in bankruptcy, as well as a shift in focus from shareholders to creditors as a company becomes insolvent).

creditors succeed in obtaining derivative standing from the bankruptcy court. This creates what Professor David Skeel calls a "black hole effect": claims are unlikely to be brought when those with the authority to bring them are also the putative defendants.[91] Indeed, at major junctures in a case, such as a sale of assets, confirmation of a plan, or conversion to chapter 7, debtors in possession typically seek exculpation of their directors and officers.[92]

Next, most big decisions in bankruptcy are subject to *ad hoc* rules, and when trustees or debtors in possession comply with those rules, courts typically find that they have complied with their fiduciary duties too.[93] One notable exception to the bankruptcy courts' conflation of rules and fiduciary duties is the requirement that the trustee select the "highest and best offer" among competing bids for estate assets.[94] While the phrase does not appear in the Bankruptcy Code itself, courts adopted it to ensure that the trustee (or debtor standing in the trustee's shoes) had complied with its fiduciary duties to consider the best interests of creditors.[95]

Even when bankruptcy decisions are not subject to any *ad hoc* rules,

[91] David A. Skeel, Jr., *Rethinking the Line Between Corporate Law and Corporate Bankruptcy*, 72 TEX. L. REV. 471, 500 (1994); *see also* Kelli A. Alces, *Enforcing Corporate Fiduciary Duties in Bankruptcy*, 56 U. KAN. L. REV. 83, 119–21, 125–27 (2007).

[92] Unlike the third-party releases in *Purdue Pharma* that are now before the Supreme Court, *see* Harrington v. Purdue Pharma, L.P., 2023 WL 5116031 at *1 (2023) (granting application for stay and writ of certiorari), no one doubts the jurisdiction or statutory authority of a bankruptcy court to exculpate directors and officers for claims relating to their conduct in the bankruptcy case.

[93] *See, e.g.*, Alces, *supra* note 91, at 84 (observing that state law actions for breach of fiduciary duties "often get lost in the application of the automatic stay, or in the provisions of a plan of reorganization, and die without receiving any sort of hearing on their merits"). "Following *Mosser*, this court has explained that a trustee acting with the explicit approval of a bankruptcy court is entitled to absolute immunity, as long as there has been full and frank disclosure to creditors and the court." *In re* Mailman Steam Carpet Cleaning Corp., 196 F.3d 1, 8 (1st Cir. 1999); *see also* Pottow, *supra* note 90, at 222 (quoting Morris v. Darrow, 341 U.S. 267, 272 (1951)).

[94] Some courts have held that a chapter 7 trustee must accept the highest monetary bid. *See, e.g.*, *In re* Flannery 974, 977 (Bankr. E.D. Pa. 1981). *But see In re* Landscape Properties, Inc., 100 B.R. 445, 447 (Bankr. E.D. Ark. 1988) ("It has been held, however, that in a liquidation case it is 'legally essential' to approve the highest offer, although this statement assumes that the offers and offerors are in all other respects comparable."). While courts today do not collapse the "highest" and "best" inquiries, they most commonly consider financial risk and any contingencies of an offer that might make it worth less than its face amount. *See, e.g.*, *In re* Family Christian, 533 B.R. 600, 622 (Bankr. W.D. Mich. 2015); *In re* Scimeca Found., Inc., 497 B.R. 753, 779 (Bankr. E.D. Pa. 2013). In these cases, the highest bids at auction included walk away provisions and suggestions that the highest bidder might be less than good for the money. *In re* Tresha-Mob, LLC, 2019 WL 1785431 at *3 (Bankr. W.D. Tex. 2019) ("Cherish's bid feels a bit Potemkin—a carefully crafted façade of independence hiding a different reality.").

[95] *See, e.g.*, *In re* Quality Stores, Inc., 272 B.R. 643, 646–47 (Bankr. W.D. Mich. 2002).

courts typically review under a standard akin to the business judgment rule, though perhaps with a little more bite to it: think of it as business-judgment-plus.[96] The broad sweep of the standard of review excuses courts from clarifying the standard of conduct.

When fiduciary duties are finally litigated in bankruptcy court, appellate review is hard to obtain. Appellate courts hesitate to disturb decisions of bankruptcy courts that have already been implemented, such as approved sales and confirmed plans, relying on doctrines of statutory and equitable mootness.[97]

Apart from the interstitial spaces where fiduciary duties may be litigated, bankruptcy law (like state law) imposes procedural and substantive hurdles to suing trustees, debtors, or their directors for monetary damages. Claims for breach of fiduciary duty may only be brought in the bankruptcy court that appointed the trustee in the first place, and some courts do not allow trustees to be sued for mere negligence.[98]

For all these reasons, several scholars have pointed out that administrative discipline may provide stronger and faster remedies for clear breaches of fiduciary duty than fiduciary duty litigation itself.[99] Indeed, a rigorous

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[96] As Professor Raymond T. Nimmer and Richard B. Feinberg point out, the more the decision impinges on the ultimate reorganization strategy, the more searching judicial review. Nimmer & Feinberg, *supra* note 20, at 18–19 (describing a sliding scale of deference); *see also* Bogart, *supra* note 18, at 223.

[97] *See, e.g.*, *In re* iE, Inc., No. CC-19-1307, 2020 WL 3547928, at *3 (B.A.P. 9th Cir. June 22, 2020) (considering four factors to determine if equitable mootness bars unwinding bankruptcy orders including "substantial consummation of the plan" and whether relief on appeal would "knock[] the props out from under the plan … creating an uncontrollable situation before the bankruptcy court"); *In re* Castaic Partners II, 823 F.3d 966, 968 (9th Cir. 2016) ("Equitable mootness concerns whether changes to the status quo … make it impractical or unequitable to unscramble the eggs."). To be fair, this reticence makes a good deal of sense. Bankruptcy courts are the emergency rooms of commercial law: the business's operations and finances need to be addressed urgently, and there is not always a way to grant an effective stay pending a lengthy appellate process.

[98] Courts have split over whether a trustee can be surcharged for mere negligence. *See, e.g.*, *In re Mailman Steam Carpet Cleaning Corp.*, 196 F.3d 1 (1st Cir. 1999) (citing cases). Regardless of the standard of liability, courts do not allow trustees to be sued without leave of the appointing court under the *Barton* doctrine, named after *Barton v. Barbour*, 104 U.S. 126 (1881). The *Barton* doctrine has two exceptions — the *ultra vires* exception and the "business exception" of 28 U.S.C. § 959(a). As for claims brought against the trustee in a personal, rather than official capacity, most claims will be subject to immunity drawn from the appointing court's judicial immunity, or under the *McNulta* doctrine. *See* McNulta v. Lochridge, 141 U.S. 327 (1891); Pottow, *supra* note 90, at 220–21; *see also*. For a sustained analysis of judicial immunity as applied to bankruptcy trustees, see generally Elizabeth H. McCullough, *Bankruptcy Trustee Liability: Is There a Method in the Madness*, 15 LEWIS & CLARK L. REV. 153 (2011).

[99] *See, e.g.*, Pottow, *supra* note 90, at 219–220; Alces, *supra* note 91, at 84–85, 131–39,

examination of fiduciary duties in bankruptcy may have been supplanted too by what Baird calls the "unwritten law of corporate reorganizations."[100] With formal fiduciary duty adjudications arising only sporadically, norm policing may be easier than enforcing legal obligations.[101]

C. Reframing the Discussion

Yet none of these reasons for neglecting fiduciary duty theory is persuasive.

As for the interstitial nature of bankruptcy fiduciary duties, not every decision in bankruptcy is subject to *ad hoc* rules. The formation of a business plan for the duration of the bankruptcy case, for example, is not subject to any formal rules in bankruptcy.[102] Apart from that, complying with the Code and complying with fiduciary duties are different obligations, and I am unaware of any legal principle that says they must be coextensive. Of course, a proposed course of action that *fails to comply* with the Bankruptcy Code surely violates the duty of care too. But the inverse is not necessarily true: just because a proposed course of action *complies* with the Bankruptcy Code does not mean that those who proposed it met their fiduciary duties.

Nor can we assume that bankruptcy norms will forestall adjudication of this issue. The notion of an "off-the-rack" business bankruptcy template, perhaps with "tailored" or "bespoke" alternatives, as Professor Laura Coordes terms it,[103] becomes much less tenable when we take seriously the inclusion of nonprofit corporations and benefit corporations as debtors under

141–44; Thomas G. Kelch, *The Phantom Fiduciary: The Debtor in Possession in Chapter 11*, WAYNE L. REV. 1323, 1366 (1992); Nimmer & Feinberg, *supra* note 20, at 71. To be sure, bankruptcy's adversarial system may provide workable control measures in big, well lawyered bankruptcies, but LoPucki's 1979–1980 study of chapter 11 cases in Missouri gives some reason for pause. Covering forty-eight chapter 11 cases, most of which were small debtors, LoPucki found that a paucity of creditors' committees, examiners, and trustees — even when the circumstances merited it. LoPucki concluded that "the debtors studied were able to continue in complete control of their businesses while they were under the jurisdiction of the court." Lynn M. LoPucki, *The Debtor in Full Control — Systems Failure Under Chapter 11 of the Bankruptcy Code? — First Installment*, 57 AM. BANK. L.J. 99 (1983); Lynn M. LoPucki, *The Debtor in Full Control — Systems Failure Under Chapter 11 of the Bankruptcy Code? — Second Installment*, 57 AM. BANK. L.J. 247 (1983).

[100] *See* BAIRD, *supra* note 16 (arguing that "[m]uch less is up in the air than it first seems").

[101] *See, e.g.*, Bogart, *supra* note 18, at 184 ("The Code grants the DIP virtually unhampered discretion in the formulation of the business plan, and provides seemingly no controls on such decisions by management."); LoPucki & Whitford, *supra* note 15, at 11.

[102] *See, e.g.*, Bogart, *supra* note 18, at 184.

[103] *See* Laura N. Coordes, Bespoke Bankruptcy, 73 FLA. L. REV. 359 (2021); *see also* Christopher D. Hampson, *Bespoke, Tailored, and Off-the-Rack Bankruptcy: A Response to Professor Coordes's "Bespoke Bankruptcy,"* 73 FLA. L. REV. F. 15 (2023).

the Code. And even as sponsors and creditors engage in hardball and creditor-on-creditor violence, it is not hard to imagine social enterprises pressing their claims in turn. Indeed, sustained discussion about whether nonprofit and benefit values might be carried into bankruptcy could help alleviate some of the stigma that, as Professor Pamela Foohey has uncovered, faces organizations like churches.[104]

Finally, while statutory and equitable mootness doctrine has long stymied efforts to align bankruptcy law across jurisdictions, the Supreme Court has recently cleared away one hurdle to appellate review of bankruptcy sales[105] and has moved quickly to preserve review of the third-party releases in the *Purdue Pharma* bankruptcy plan, signaling a willingness to adjust procedures to resolve thorny bankruptcy issues.[106] If appellate courts follow suit, we may witness a new wave of helpful bankruptcy precedent[107] — perhaps even concerning fiduciary duties.

III. THE TRUSTEE

Now on to the core of the problem: who are the most important bankruptcy fiduciaries and what is the content of their fiduciary duties?

We start with the trustee.[108] The trustee in bankruptcy is the "representative of the estate" and "has capacity to sue and be sued."[109] A disinterested, competent individual may serve as trustee, or the role may be filled by a corporation authorized in its charter or bylaws to serve or, if necessary, the U.S. Trustee.[110] In chapter 7 and chapter 11 cases, trustees are

[104] *See* Pamela Foohey, *When Faith Falls Short: Bankruptcy Decisions of Churches*, 76 OHIO ST. L.J. 1319 (2015) (drawing on interviews with forty-five religious leaders). For Foohey's empirical analyses of religious organization bankruptcy cases, see Pamela Foohey, *When Churches Reorganize*, 88 AM. BANK. L.J. 277 (2014); Pamela Foohey, *Bankrupting the Faith*, 78 MO. L. REV. 719 (2013).

[105] MOAC Mall Holdings v. Transform Holdco LLC, 598 U.S. 288, 936–37 (2023) (holding § 363(m) is not jurisdictional).

[106] Harrington v. Purdue Pharma, L.P., 2023 WL 5116031 at *1 (2023) (granting application for stay and writ of certiorari).

[107] *See* Bogart, *supra* note 18, at 1–2.

[108] Seasoned students of bankruptcy might expect us to start with the debtor in possession. As I will cover more in depth below, *see infra* Section IV.B, a prominent feature of U.S. bankruptcy practice since the 1978 Code has been allowing the debtor's old management to manage and operate the business in bankruptcy. But as I am advancing a doctrinal and technical approach in this Article, we must start with the trustee — both because some bankruptcy cases do not have a debtor in possession at all, and because, when they do, the debtor in possession wears the trustee's cap.

[109] 11 U.S.C. § 323. As noted above, the *Barton* doctrine applies to trustees in bankruptcy. *See supra* note 98 and accompanying text.

[110] 11 U.S.C. § 322. The U.S. Trustee's Office falls within the Department of Justice.

elected by creditors.[111] In chapters 12 and 13, the U.S. trustee appoints the bankruptcy trustee.[112] In any kind of case, the trustee has leeway to conduct business as usual, but must seek court approval for any kind of use, sale, or lease of property that is outside the "ordinary course of business."[113]

Bankruptcy trustees can play very different roles, depending on the chapter under which the case is proceeding. In this Part, I describe the statutory duties of each kind of trustee, analyze the nature and scope of their fiduciary duties, and argue that the fiduciary duties of the trustee account for the special purpose of nonprofits and benefit corporations, or something we might call corporate character.

A. Statutory Duties

In all bankruptcy cases, the trustee has four statutory duties: to account for any property received; to review claims against the estate and object to any improper claims; to provide information about the estate and its administration to parties in interest that request it; and to prepare a final report.[114] Other duties depend on the chapter and the circumstances.

1. The Liquidating Trustee

Chapter 7 of the Bankruptcy Code covers what many laypeople imagine bankruptcy to be: liquidation. The Code directs a chapter 7 trustee to "investigate the financial affairs of the debtor" and "collect and reduce to money the property of the estate … and close such estate as expeditiously as is compatible with the best interests of parties in interest."[115]

But that does not mean that a liquidation must happen precipitously. The court may authorize the trustee to "operate the business of the debtor for a limited period" if doing so is in the "best interest of the estate" and "consistent with the orderly liquidation of the estate."[116]

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[111] *Id.* § 702; 1104(b)(1).

[112] *Id.* §§ 1202(a); 1302(a).

[113] *Id.* § 363(b)(1).

[114] These duties come from 11 U.S.C. § 704(a)(2), (5), (7) and (9), each of which is incorporated into chapter 11 by section 1106 of the Code, and in subchapter V by section 1183(b)(1). As Pottow points out, the trustee's ability to object to the validity, size, priority, or secured status of claims "thrust[s] trustees into an *antagonistic* posture with the natural beneficiaries to whom they owe a duty of loyalty." Pottow, *supra* note 90, at 209; *see also id.* at 210–11. Subsections (a)(3), (a)(6), and (a)(10) of 11 U.S.C. § 704 apply only in individual cases.

[115] 11 U.S.C. § 704(a)(1).

[116] *Id.* § 721. If the court does so, the trustee is responsible for filing any tax paperwork.

2. The Reorganizing Trustee

By contrast, chapters 11, 12, and 13 of the Bankruptcy Code provide for various kinds of repayment or reorganization plans.

Under Chapter 11, if the business has a solid economic plan, the fact that it is facing financial distress need not destroy any go-forward value. Instead, while the trustee operates the estate,[117] the debtor may propose a plan of reorganization. As in chapter 7, the Code directs a chapter 11 trustee to investigate the debtor, with special attention paid to anything relevant to the "formulation of a plan."[118]

At the beginning of a chapter 11 case, only the debtor may file a plan. When the debtor loses its exclusive rights to file a plan, the chapter 11 trustee must file a plan "as soon as practicable" — or, alternatively, a report of why the trustee thinks the case should be dismissed or converted to a chapter 7 liquidation.[119] In chapter 12 and 13 bankruptcies, which have as their aim a three- to five-year repayment plan, the trustees also ensure that the debtor starts (and continues) making payments under the plan.[120]

Subchapter V (pronounced "five") is the newest pathway through bankruptcy for small business debtors in chapter 11.[121] It provides an attractive and streamlined repayment model for small businesses and their owners. For business debtors, the subchapter V trustee has many of the same duties as a regular chapter 11 trustee: it may operate the business of the

Id. § 704(a)(8). The trustee also must serve as the administrator of any employee benefit plan and, if the estate is closing a health care business, must use "all reasonable and best efforts" to transfer patients to an appropriate alternative. *Id.* § 704(a)(11) and (12).

[117] Indeed, in chapter 11, the trustee does not need to seek Court permission to operate the business: the Code authorizes the trustee to do so unless a party requests otherwise and the court agrees. 11 U.S.C. § 1108 ("Unless the court, on request of a party in interest and after notice and a hearing, orders otherwise, the trustee may operate the debtor's business.").

[118] 11 U.S.C. § 1106(a)(3). The trustee must also file a summary of its investigation and send a copy to any creditors' committee and equity security holders' committee. *Id.* § 1106(a)(4). If a plan is confirmed, the trustee must file any necessary post-confirmation reports. *Id.* § 7.

[119] 11 U.S.C. § 1106(a)(5).

[120] 11 U.S.C. §§ 1202(b)(4)–(5); 1226; 1302(b)(4)–(5); 1326.

[121] For recent discussions of how subchapter V may affect bankruptcy strategy, see Christopher D. Hampson & Jeffrey A. Katz, *The Small Business Prepack: How Subchapter V Paves the Way for Bankruptcy's Fastest Cases* (GEO. WASH. L. REV., forthcoming 2024); Christopher G. Bradley, *The New Small Business Bankruptcy Game: Strategies for Creditors Under the Small Business Reorganization Act*, 28 AM. BANKR. INST. L. REV. 251 (2020); Brook E. Gotberg, *Reluctant to Restructure: Small Businesses, the SBRA, and COVID-19*, 95 AM. BANKR. L.J. 389 (2021); Nicole C. Cipriano, *The Big Short: How the Big Step of the Small Business Reorganization Act Fell Short*, 50 HOFSTRA L. REV. 145 (2021).

debtor, for example.[122] Yet the job description is more conciliatory than a chapter 11 trustee's usual role. The subchapter V trustee is charged with "facilitat[ing] the development of a consensual plan of reorganization"[123] and conducts investigations and files post-confirmation reports only if a party requests it and the court agrees.[124]

B. Fiduciary Duties

While the trustee's statutory duties are set forth exhaustively in the Code, its fiduciary duties are nowhere mentioned. Yet bankruptcy courts (and the U.S. Trustee's Office) have uniformly concluded that the statutory duties of the trustee[125] give rise to fiduciary duties to the estate and its beneficiaries.[126] The conclusion seems inevitable, even though, as Pottow has pointed out, some of the statutory duties set the trustee in an adversarial role against

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[122] 11 U.S.C. § 1183(b)(5)(B).

[123] *Id.* § 1183(b)(7).

[124] *Id.* § 1183(b)(2).

[125] Of course, any professionals (including lawyers) that the trustee may hire under sections 327, 1103 or 1114 of the Code also owe fiduciary duties to the estate. *See, e.g.*, *In re Grabill Corp.*, 113 B.R. 966, 970 (Bankr. N.D. Ill. 1990) ("This principle of fiduciary duties and obligations carries over to the attorneys and the other professionals listed in Bankruptcy Rule 2014(a) who are retained for the debtor-in-possession.") (citing Fed. R. Bankr. P. 2014(a)); *see also* Rapoport & Boyles, *supra* note 78, at 59–60.

[126] Indeed, the Supreme Court has said as much in at least three important cases extending back through the life of the Bankruptcy Code and its predecessor, the Act. *See* Pepper v. Litton, 308 U.S. 295 (1939) (noting that trustees have fiduciary duties "designed for the protection of the entire community of interests of the corporation — creditors as well as stockholders"); Wolf v. Weinstein, 372 U.S. 633, (1963); CFTC v. Weintraub, 471 U.S. 343, 355-56 (1985); *see also* Lubben, *supra* note 46, at 4 7 nn. 7–8 (collecting cases); Steven Rhodes, *The Fiduciary and Institutional Obligations of a Chapter 7 Bankruptcy Trustee*, 80 AM. BANK. L.J. 147, 154 & n.35 (2006) (collecting cases).

The U.S. Trustee's office mentions that the trustee has fiduciary responsibilities throughout its Chapter 7 Handbook, though it does not expound on the nature or source of those duties. *See* U.S. DEP'T OF JUSTICE, EXECUTIVE OFFICE FOR U.S. TRUSTEES, HANDBOOK FOR CHAPTER 7 TRUSTEES 1-2, 2-3, 2-8, 4-2, 4-26, 4-31, 5-1, 5-2, 6-1, 6-2 (2012), www.justice.gov/ust/private-trustee-handbooks-reference-materials [hereinafter "CHAPTER 7 TRUSTEE HANDBOOK"]. The Chapter 7 Trustee Handbook specifies that the section 704 duties are "specific, but not exhaustive," pointing to the supervisory obligations of the U.S. Trustee's Office over chapter 7 trustees. *See id.* at 4-2 (citing 28 U.S.C. § 586)). The same cursory usage of the phrase repeats in the Chapter 11 Handbook and the Subchapter V Handbook. *See* U.S. DEP'T OF JUSTICE, CHAPTER 11 TRUSTEE HANDBOOK 1, 6, 15, 16, 19, 70, 73, 74 (2004), www.justice.gov/ust/private-trustee-handbooks-reference-materials [hereinafter "CHAPTER 11 TRUSTEE HANDBOOK"]; U.S. DEP'T OF JUSTICE, EXECUTIVE OFFICE FOR U.S. TRUSTEES, HANDBOOK FOR SMALL BUSINESS CHAPTER 11 SUBCHAPTER V TRUSTEES 1-5, 1-7, 2-1, 2-2, 3-8, 4-3 (2020), www.justice.gov/ust/private-trustee-handbooks-reference-materials [hereinafter "SUBCHAPTER V TRUSTEE HANDBOOK"].

certain creditors.[127]

But bankruptcy courts vary widely in their articulation of the source and content of those fiduciary duties. They disagree over whether the source of the trustee's fiduciary obligations comes from federal law or state law. Since the trustee is a federal officer, and the bankruptcy estate is the creation of a federal statute, one might naturally think that federal law would govern.[128] "[W]hat right does state law have to intrude on such an essential aspect of (federal) chapter 11 procedure?," asks Lubben.[129] Pottow, too, describes bankruptcy courts as applying a general common law of trusts.[130]

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[127] Pottow categorizes the duties as fiduciary, non-fiduciary, and anti-fiduciary. *See* Pottow, *supra* note 90, at 208–11; *see also* Brook E. Gotberg, *Relational Preferences in Chapter 11 Proceedings*, 71 OKLA. L. REV. 1013, 1053 (2019) (noting that the fiduciary duty to pursue preference actions may involve "engaging in potentially self-destructive actions"). Other commentators have categorized the duties differently. Bankruptcy Judge Steven W. Rhodes separates the trustee's "fiduciary" obligations to the court and parties in specific cases from the trustee's "institutional obligations to the bankruptcy process itself, noting that the two types of obligations may conflict. *See* Rhodes, *supra* note 126, at 147–48. Professor Elizabeth McCullough labels them "functionary" and "fiduciary." *See* McCullough, *supra* note 98, at 162. Indeed, in large part due to the adversarial nature of bankruptcy, Professor Kelch proposes getting rid of DIP fiduciary duties altogether, relying on the debtor's preexisting fiduciary duties under state corporate law. *See* Kelch, *supra* note 99, at 1364.

The scholarly literature and caselaw divides on whether the trustee owes fiduciary obligations to creditors as a whole or to all potential stakeholders in the estate, including equity shareholders. *See, e.g.*, Rapoport & Bowles, *supra* note 78, at 52–54; LoPucki & Whitford, *supra* note 90, at 709 (concluding that management "owes" fiduciary duties to both creditor and shareholders until their claims and interests are "extinguished" in the bankruptcy case). For a particularly expansive description of the scope of the trustee's obligations, *see* Lynn M. LoPucki, *A Team Production Theory of Bankruptcy Reorganization*, 57 VAND. L. REV. 741 (2004) [hereinafter LoPucki, *Team Production Theory*].

[128] Lubben, for example, posits that the DIP (who undertakes the trustee's duties, *see infra* Section IV.B), takes on "new obligations that are functions of federal law." Lubben, *supra* note 46, at 25; *see also In re Signature Apparel Grp. LLC*, 577 B.R. 54, 96–97 (Bankr. S.D.N.Y. 2017) (noting that the fiduciary duty of loyalty in bankruptcy had "aris[en] under federal law"). This assumption, however, creates what Skeel identifies as *vestigialization*: state lawmakers ignore insolvency issues because they believe that the federal government is handling it; federal bankruptcy courts, in turn, look to state law for resolution of many issues not addressed specifically by the Code. *See* Skeel, *supra* note 91, at 489–90. Indeed, Professors Henry Hu and Jay Westbrook's proposal to abolish duty shifting under state law would create even *more* vestigialization — since it would send consideration of fiduciary duties to creditors over to bankruptcy court, where the precise nature of those duties might turn on state law. *See* Henry T.C. Hu & Jay Lawrence Westbrook, *Abolition of the Corporate Duty to Creditors*, 107 COLUM. L. REV. 1321 (2007).

[129] Lubben, *supra* note 46, at 30.

[130] *See* Pottow, *supra* note 90, at 211 (quoting *United States ex rel. Willoughby v. Howard*, 302 U.S. 445, 450 (1938)); *see also* Daniel B. Bogart, *Unexpected Gifts and Chapter 11: The Breach of a Director's Duty of Loyalty Following Plan Confirmation and*

But nothing in the Bankruptcy Code sets forth a federal standard for the fiduciary duties of the trustee, and longstanding federalism principles, most famously captured by *Butner v. United States*,[131] suggest that courts ought to backfill any omissions in the Code by referring to state law, absent some strong federal interest.[132] Hence, other commentators, such as prominent restructuring attorney Martin Beinenstock, assume that state law governs.[133]

Courts also disagree over whether the content of the duties comes from trusts, corporations, agency, or something *sui generis*.[134]

The Bankruptcy Code is, of course, shot through with references to the trustee and the estate. Indeed, when individuals file for bankruptcy, no corporate governance could conceivably apply. Similarly, the process for appointment of trustees seems to indicate their allegiance to the beneficiaries of the estate: the creditors. Bogart thus argues that the bankruptcy courts have developed a federal "common law of trusts."[135] Bankruptcy courts refer to the trustee's duty to "maximize the value of the estate"[136] and to act in the best interests of the estate's beneficiaries, usually the creditors. The section 363 "highest and best offer" standard arose from state law disputes over trustee or executor sales.[137]

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the Postconfirmation Jurisdiction of Bankruptcy Courts, 72 AM. BANK. L.J. 303, 312 (1998) ("The federal bankruptcy trustee is a creation of national law in the service of a Code that reaches across all state lines: creditors may reasonably expect trustees from different jurisdictions to be governed by the same standard, worded the same.").

[131] 440 U.S. 48 (1979).

[132] *Id.* at 55; *see also* Rodriguez v. Fed. Deposit Ins. Corp., 140 S. Ct. 713, 717 (2020); Erie R. Co. v. Tompkins, 304 U.S. 64 (1938).

[133] *See* Martin J. Bienenstock, *Conflicts Between Management and the Debtor in Possession's Fiduciary Duties*, 61 U. CIN. L. REV. 543, 551 (1992) (concluding that state law governs fiduciary duties in bankruptcy); *see also* Hill v. Portillo (*In re* Kenneth C. Casey, Inc.), 2022 WL 2198882 (Bankr. D. Colo. 2022) (same).

[134] *See* Roache, *supra* note 78, at 134 (describing the corporation theory as the majority view in the caselaw); Rapoport & Bowles, *supra* note 78, at 55–56 (same). Some commentators and courts seem to suggest that, for most actual controversies, either standard would reach the same outcome. *Id.* at 56–57 (noting that in the *Schipper* bankruptcy, the bankruptcy court, district court, and court of appeals all noted that their opinion on a section 363 sale would have been the same under either the trust or corporate doctrines) (citations omitted); Frost, *supra* note 19, at 120 ("The standards existing inside of bankruptcy do not differ much from the standards outside of the process").

[135] *See, e.g.*, Daniel B. Bogart, *Finding the Still Small Voice: The Liability of Bankruptcy Trustees and the Work of the National Bankruptcy Review Commission*, 102 DICK. L. REV. 703, 709 (1998); United States v. Aldrich (*In re* Rigden), 795 F.2d 727 (9th Cir. 1986); *In re Christensen*, 2020 WL 2027232 (Bankr. D. Utah 2020) (noting that bankruptcy courts have "fashioned a common law of trusts").

[136] *See, e.g.*, CFTC v. Weintraub, 471 U.S. 343 (1985); United States v. Aldrich (*In re* Rigden), 795 F.2d 727 (9th Cir. 1986).

[137] *See, e.g.*, Camden v. Plain, 4 S.W. 86, 88 (Mo. 1886); Tillman v. Dunman, 40 S.E.

Yet bankruptcy courts also commonly use the language of deference, reviewing the trustee's actions under what they say is the "business judgment rule," a standard that has no parallel in trust law.[138] Accordingly, some scholars, like Lubben, advocate for the use of "a kind of common law of corporations" in bankruptcy.[139]

Either way, a few starting premises are clear. First, the Bankruptcy Code must be a source of law for some bankruptcy fiduciary duties. For while businesses have preexisting fiduciary duties that the Code might borrow for bankruptcy purposes, no such state law analog exists for consumer cases.

Second, Congress could spell out the fiduciary duties of the trustee, designing a federal list of duties or requiring that bankruptcy trustees follow any fiduciary duties that governed the debtor under state law.[140] It could also (probably) delegate the issue to the U.S. Trustee's Office or the DOJ.[141] Congress has done this in other contexts, such as for the fiduciary duties that apply to ERISA accounts.[142] It has not been as clear in the Bankruptcy Code.

244, 245 (Ga. 1901); Angevine v. Sesser, 39 F. Supp. 498, 501 (E.D. Ill. 1941). Trustees or executors used the term as a defense or justification for a sale of trust assets. In contract law, judges could swiftly end disputes about adequate consideration or remedial measures by pointing to the fact that the bid accepted was the highest and best offer. Bankruptcy courts widely adopted the formulation in the 1980s. *See In re* New York, S. & W. R. Co., 511 F. Supp. 625, 628 (D.N.J. 1981); *In re* WFDR, Inc., 10 B.R. 109, 109 (Bankr. W.D. Ga. 1981); Jandel v. Precision Colors Inc., 19 B.R. 415, 419 (Bankr. S.D. Ohio 1982); *In re* Shougar, 1988 Bankr. LEXIS 1859 at *2 (Bankr. S.D. Fla. 1988).

[138] *See, e.g.*, *In re* Johns-Manville, 60 Br. 612, 615–16; Nimmer & Feinberg, *supra* note 20, at 13 (describing the "business judgment" test as the governing standard for decisions within the ordinary course); Rhodes, *supra* note 126, at 171 (describing bankruptcy courts' use of business judgment review); Bogart, supra note 18, at 164–65 (criticizing use of corporate theory); Kelch, *supra* note 99, at 1341–43 (same).

Sorting out the standard of review still leaves some unsolved puzzles. For example, should state laws allowing corporations to exculpate their directors and officers from breaches of the duty of care similarly exculpate the trustee in bankruptcy? At least some scholars think the answer must be no. *See id.* at 239–40; Lubben, *supra* note 46, at 30. What fiduciary obligations should govern trustees and DIPs after the confirmation of a plan? *See generally* Bogart, *supra* note 130.

[139] Lubben, *supra* note 46, at 31.

[140] *See* U.S. CONST. art. I, § 8, cl. 4 (granting Congress the power to "establish … uniform Laws on the subject of Bankruptcies throughout the United States). Congress could certainly preempt state law on the subject.

[141] Whether Congress has delegated resolution of this question to the U.S. Trustee's Office or the Department of Justice is another curiosity worth exploring. One wonders whether the courts would presume that Congress has done so, even with the Supreme Court's new major questions doctrine. *See* West Virginia v. EPA, 142 S. Ct. 2587 (2022). Even if Congress meant to delegate to the UST or the DOJ, those agencies have not resolved the issue so far, whether through informal guidance or notice-and-comment rulemaking.

[142] *See* 29 U.S.C. § 1104 (setting forth statutory and fiduciary duties to govern managers of ERISA plans).

Nor have the U.S. Trustee's Office and DOJ taken up the question of the trustee's fiduciary duties in any granularity.

C. A Space for Corporate Character

The stakes of the fiduciary duty question are no less than the purpose of bankruptcy itself. Is bankruptcy a one-size-fits-all procedure, where the various missions of corporate entities are collapsed into a uniform treatment? Or does the bankruptcy process require trustees to accommodate the different fiduciary obligations that apply to nonprofit organizations and benefit corporations? And if bankruptcy fiduciary duties account for state-law variation, does it accommodate the "enhanced" fiduciary duties of nonprofits and benefit corporations only, or does it also accommodate fiduciary waivers? To resurrect our metaphor from the introduction, the trustee of Green Creek needs to understand whether it can keep the green trucks on the roads or whether it should convert to the more profitable brown trucks.

My own view is that the duties of obedience or balancing should persist into insolvency and bankruptcy.[143] Drawing from virtue ethics and the channeling function of law, I have previously advanced an understanding of corporate identity, culture, and character that allows for a more expansive vision of profit-seeking to guide the life cycle of a corporation, even (and especially) in bad times.[144] In this section, I advance two arguments for why the bankruptcy trustee must follow enhanced fiduciary duties in bankruptcy under the law as it currently stands.

1. The Purpose of the Bankruptcy Estate

First, the trustee in bankruptcy, like any trustee, has a duty to manage and operate the estate in accordance with the trust instrument — part of the duty of obedience.[145] Here, the closest analog to the trust instrument is not a will, a grant, or articles of incorporation, but the Bankruptcy Code itself, since it is the Code that creates the estate.

The Code, as we have seen, envisions different purposes for the estate under different chapters. The purpose of a chapter 7 case is an orderly liquidation. The trustee's duty of obedience in a chapter 7 bankruptcy thus includes a duty to "maximize the value of the estate" — which is why the

[143] See Hampson, *supra* note 7.
[144] *Id.* at 124–28.
[145] *See supra* note 58 and accompanying text. Section 959 might factor into this puzzle as well. In *Alonso v. Weiss*, 932 F.3d 995 (7th Cir. 2019), the Seventh Circuit, relying on section 959, analyzed what fiduciary obligations the law of Illinois would impose on a court-appointed trustee..

Supreme Court in *Weintraub* cited the first statutory duty of a chapter 7 trustee, the duty to "collect and reduce to money the property of the estate for which such trustee serves."[146] But that statutory duty does not apply to chapters 11, 12, or 13 cases, and thus the formulation of "maximize value" does not apply under those cases either.

By contrast, the purpose of chapter 11, 12, and 13 cases is to reach a reorganization or repayment plan, where possible.[147] Under these chapters, then, the purpose of the trust is to preserve go-forward value through a confirmed repayment plan or a plan of reorganization. Of course, the trustee does not have the power to propose a plan in the first instance — the debtor has a right of exclusivity. Accordingly, we might say that the trustee's duty of obedience gives rise to a "duty to facilitate" or a "duty to clear runway" for the parties to negotiate a plan.[148] What this means, of course, is that the trustee in bankruptcy should preserve the trust corpus, the *res*, to allow the parties to negotiate and vote on a plan. The trustee should not cause the estate of a nonprofit debtor to deviate from its charitable mission, nor should it cause the estate of a benefit debtor to abandon the public benefit it is meant to balance. The trustee of Green Creek's estate should keep the green trucks on the road, for now.

2. Bankruptcy's Preemption "Saving Clause"

Second, 28 U.S.C. § 959 — what Professor Robert Miller calls bankruptcy's preemption "saving clause" — may direct trustees to follow the state law fiduciary duties of their debtor.[149] Section 959 states:

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[146] *C.F.T.C. v. Weintraub*, 471 U.S. 343, 352 (1985) (citing 11 U.S.C. § 704(a)(1)).

[147] *See, e.g.*, Gotberg, *supra* note 127, at 1018 ("The DIP's fiduciary duty to maximize the estate certainly suggests a duty to maximize preference recoveries pursuant to a cost-benefit analysis, although there is no clear direction on how costs and benefits should be measured."). This discretionary space can create unintended consequences. Professor Gotberg, in a set of forty-eight interviews (creditors, debtors, and attorneys), demonstrated that creditors had incentives to make pre-bankruptcy preference payments for leverage during a later bankruptcy proceeding, and, for their part, that debtors saw preference litigation as leverage too, rather than through the lens of fiduciary duty. Gotberg concludes that preference litigation can be better understood as "a tool to manage business relationships in bankruptcy." *See id.* at 1021.

[148] Under these chapters, the trustee's obligation is akin to the subsection V trustee, in small business cases, to "facilitate the development of a consensual plan of reorganization."

[149] Robert Miller, *A Comprehensive Framework for Conflict Preemption in Federal Insolvency Proceedings*, 123 W. VA. L. REV. 423, 426 (2020). In his article, Miller sets forth a comprehensive framework for preemption in bankruptcy, arguing that the function of 28 U.S.C. § 959 is to "eliminat[e] obstacle preemption when it is triggered in a federal insolvency proceeding." *Id.* at 428; *see also id.* at 465–67 (setting forth Miller's proposed test in verbal and flowchart form).

> (a) Trustees, receivers or managers of any property, including debtors in possession, may be sued, without leave of the court appointing them, with respect to any of their acts or transactions in carrying on business connected with such property. Such actions shall be subject to the general equity power of such court so far as the same may be necessary to the ends of justice, but this shall not deprive a litigant of his right to trial by jury.
>
> (b) Except as provided in section 1166 of title 11, a trustee, receiver or manager appointed in any cause pending in any court of the United States, including a debtor in possession, shall manage and operate the property in his possession as such trustee, receiver or manager ***according to the requirements of the valid laws of the State in which such property is situated, in the same manner that the owner or possessor thereof would be bound to do if in possession thereof.***[150]

As a matter of text, section 959(b) seems to require the trustee to follow state law fiduciary duties. To be fair, though, the case that section 959 resolves the issue is not that straightforward. To start, courts differ on whether the statute applies to chapter 7 liquidations at all, since chapter 7 trustees do not usually "operate" the business of the debtor.[151]

Let's begin with the text of section 959. We must first ask whether fiduciary obligations are the kind of "laws" to which the statute refers. Surely fiduciary obligations, as an offshoot of agency law, usually count as "law,"[152] but when courts have examined subsection (a), which allows trustees to be sued in any court with jurisdiction for their "acts or transactions in carrying on business" (an exception to the *Barton* doctrine that trustees may only be sued in the appointing court), they have concluded that section 959(a) does

[150] 28 U.S.C. § 959 (emphasis added). Miller's discussion of section 959 is the most thorough discussion in the literature, *see supra* note 149, but while he cleans up much of the confusion and provides a workable framework for applying the law, his article doesn't address the puzzle of fiduciary duties. Even so, I am not alone in my conclusion that section 959(b) means that benefit corporation debtors and trustees in bankruptcy must follow the state benefit corporation legislation. Russell C. Silberglied has made the same argument. *See* Russell C. Silberglied, *Can a Lower Bid for a Debtor's Assets Be Approved as "Better" Because It Saves More Jobs than the Higher Bid?*, 76 BUS. LAW. 817, 837–38 (2021).

[151] *See, e.g.*, Rhodes, *supra* note 126, at 189–90 & nn.194–95 (describing a circuit split on whether section 959 covers chapter 7 liquidations); *In re* Borne Chemical Company, Inc., 54 B.R. 1236 (Bankr. D.N.J.); *In re* Valley Steel Products Co., Inc., 157 B.R. 442 (1993). Miller thinks that the minority position has it correct: section 959(b) applies not just to reorganizing trustees but also liquidating trustees, since they either "operate" or "manage" the estate. *See* Miller, *supra* note 149, at 476–78.

[152] *See, e.g.*, David J. Seipp, *Trust and Fiduciary Duty in the Early Common Law,* 91 B.U. L. REV. 1011, 1034–36 (2011).

not apply to claims for breach of fiduciary duty.[153] Of course, subsection (b) might sweep more broadly than subsection (a), but a reasonable interpretation of the two subsections put together is that they refer to the trustee's external obligations, not the obligations that the trustee owes to the estate and its beneficiaries.[154]

Another wrinkle is that section 959(b) directs the trustee to follow the "valid laws of the State in which such property is situated." If it includes fiduciary duties, wouldn't section 959(b) bind a trustee to a dizzying kaleidoscope of fiduciary duties, all based on where the property is located? Such a concern is, I think, overstated: state choice-of-law doctrine should point the trustee either to the law of the appointing court (trust law) or the state of incorporation (corporate law).[155] In any event, courts have already applied section 959 to tort and contract, where the governing law does not turn on the location of property.[156]

The legislative history of the provision is not much help. Originally, Congress wanted to clarify that federal trustees, receivers, and managers of property were not exempt from paying state taxes.[157] And yet it would have been easy to draft a statute limited to taxation, so courts have applied the statute to state regulations generally, allowing state law to impose restrictions

[153] *See In re* Lehal Realty Assoc., 101 F.3d 272 (2d Cir. 1996); *In re* McKenzie, 476 B.R. 515 (E.D. Tenn. 2012); Kashani v. Fulton (*In re* Kashani), 190 B.R. 875 (B.A.P. 9th Cir. 1995); *In re* East Coast Foods, Inc., 2023 WL 4626782 (B.A.P. 9th Cir. 2023).

[154] Careful statutory readers will look for a clue in the exception for 11 U.S.C. § 1166. That provision, which was added in 1978, requires the trustees of railroads to follow the federal rules in Title 49 that govern railroads. Those provisions are operational rules, not fiduciary duties. But a carveout to ensure that trustees of railroads follow federal regulations does not seem to weigh heavily either way on whether the rest of section 959(b) covers fiduciary duties or not.

[155] *See, e.g.*, Rogers v. Guar. Tr. Co. of New York, 288 U.S. 123, 130 (1933) ("It has long been settled doctrine that a court — state or federal — sitting in one State will as a general rule decline to interfere with … the management of the internal affairs of a corporation organized under the laws of another state but will leave … such matters to the courts of the state of the domicile.").

[156] *See* Reading Co. v. Brown, 391 U.S. 471 (1968); *see also* Mission Product Holdings v. Tempnology, 139 S. Ct. 1652 (2019) (noting that a debtor does not get "an exemption from all the burdens that generally applicable law — whether involving contracts or trademarks — imposes on property owners").

[157] *See* Palmer v. Webster & Atlas Nat. Bank of Boston, 312 U.S. 156 (1941). And indeed, this background helps make some sense of the reference in section 959(b) to the "valid laws of the State in which such property is situated." 11 U.S.C. § 959(b).

on a trustee's ability to abandon,[158] sell,[159] or operate[160] the estate's property. A handful of courts have even applied section 959 to fiduciary duty law.[161]

Reasonable minds may differ on the proper interpretation of this statute. On this view, 28 U.S.C. § 959 directs trustees to manage or operate the estate in accordance with the fiduciary duties that would govern the debtor had the debtor not filed for bankruptcy. For individual debtors, section 959 does not impose any additional fiduciary duties. For business debtors, though, section 959 imposes additional fiduciary duties stemming from state law. This result is consistent with how courts have applied section 959 over the years, broadening its scope beyond the original application of taxes to encompass contract and tort. It is also consistent with the Supreme Court's longstanding direction, reflected in cases like *Erie* and *Butner*, to incorporate state law absent strong federal indications to the contrary.[162]

3. Problems and Puzzles

How do the duties of obedience, balancing, or plan facilitation affect the trajectory of reorganization cases?

First, trustees in bankruptcy that manage or operate the bankruptcy estate must undertake that task consistently with the organization's purpose. A bankruptcy trustee managing the estate of a nonprofit or benefit corporation, therefore, should not assume that the pro-social commitments of those organizations ought to vanish during the pendency of the bankruptcy case. In a chapter 11 case, Green Creek's trustee must keep the green trucks on the road, so long as a plan of reorganization is in the works. That result is buttressed by the Code's deference given to the trustee: if the decisions are in the ordinary course, notice and a hearing need not be provided.[163]

Second, wherever possible, the trustee should attempt to manage the estate in a manner consistent with preserving go-forward value in the

[158] *See, e.g.*, Midatlantic National Bank v. New Jersey Dept. of Environ. Protection, 474 U.S. 494 (1986); Palmer v. Commonwealth of Massachusetts, 308 U.S. 79 (1939).

[159] *See, e.g.*, *In re* White Crane Trading Co., Inc., 170 B.R. 694 (Bankr. E.D. Cal. 1994).

[160] *See, e.g.*, Gillis v. California, 293 U.S. 62 (1934) (licenses to distribute motor vehicle fuel); Clancy v. Goldberg, 183 B.R. 672 (N.D.N.Y. 1995) (placing advances in escrow); *In re* Investors Development Co., 7 B.R. 772 (Bankr. D.N.J. 1980) (improvements to real property mandated by a town); *see also* Rhodes, *supra* note 126, at 191 (cataloguing cases applying section 959 to "environmental regulations, tax law requirements, pension plan termination requirements, and Federal Arbitration Act obligations) (internal citations omitted).

[161] *See* Alonso v. Weiss, 932 F.3d 995 (7th Cir. 2019); County of Oakland by Kuhn v. City of Detroit, 784 F. Supp. 1275 (E.D. Mich. 1992).

[162] *See, e.g.*, Butner v. United States, 440 U.S. 48, 55 (1979); Rodriguez v. Fed. Deposit Ins. Corp., 140 S. Ct. 713, 717 (2020); Erie R. Co. v. Tompkins, 304 U.S. 64, __ (1938).

[163] *See* 11 U.S.C. § 363(c).

company. That means, at a minimum, not dramatically altering the business's practices while a plan of reorganization is still viable. A viable plan of reorganization may require the stakeholders who initially formed the corporation to maintain their enthusiasm for the reorganized corporation. While a plan is in the works, the trustee may not liquidate the estate in countervailing ways.

Third, bankruptcy trustees should ignore diminished or waived fiduciary duties for LLC or LP debtors. This result is consistent with what the handful of courts to have addressed the issue conclude, though for different reasons.[164] Under this Article's "duty to facilitate" or a "duty to clear runway" theory, the trustee's fiduciary duties flow directly from the Code itself, and state law variation or individualized waivers have no relevance. While section 959 requires the trustee to follow state law fiduciary duties, it doesn't purport to relieve the trustee from its duties under federal law.

Finally, reorganizing trustees should hesitate to sell the entire company under section 363 of the Code. Bankruptcy aficionadas will note that, as a formal matter, the *trustee*, not the debtor, has power to sell assets of the estate under section 363.[165] Since, in my view, the reorganizing trustee has a duty to facilitate a plan, asset sales of the company may improperly truncate the plan negotiation process. Indeed, bankruptcy courts typically require a "good business reason" for a section 363 sale,[166] a rule that helps ensure that sales do not entirely replace plans as the end destination of bankruptcy cases.[167]

Similarly, since the trustee must follow state law fiduciary duties, any section 363 sales must comply with the duty of obedience and the duty of balancing, if applicable — subject, of course, to the fact that insolvency may

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[164] For example, in *In re Houston Regional Sports Network*, the Astros argued that the bankruptcy should be dismissed because the Astros, one of the partners in the debtor, held veto power over any plan of reorganization and would exercise that power to ensure that no plan could be confirmed. In re *Houston Reg'l Sports Network, L.P.*, 505 B.R. 468, 479 (Bankr. S.D. Tex. 2014). Citing *Weintraub*, the court held that the Bankruptcy Code imposed fiduciary duties upon the Astros and signaled that it would hold them to those duties; thus, it could not exercise its veto power for selfish reasons. *See id.* at 481 ("As in *Weintraub*, this Court holds that the fiduciary duties to a bankruptcy estate may not be absolved by any state-law concepts to the contrary.").

[165] 11 U.S.C. § 363.

[166] *In re* Chrysler LLC, 576 F.3d 108 (2d Cir. 2009); Comm. of Equity Sec. Holders v. Lionel Corp. (*In re* Lionel Corp.)¸ 722 F.2d 1063, 1071 (2d Cir. 1983) (allowing a sale when the assets were "of a perishable nature or liable to deteriorate in value" and requiring a "boos business reason").

[167] The fact that bankruptcy courts nonetheless approve such sales reflects, I think, the fact that in such cases (at least, every case of which I am aware) the debtor is serving as the trustee, and the debtor has a right to propose a plan and, correspondingly, a right to convert the case to chapter 7. If, by contrast, a separate chapter 11 trustee had been appointed, surely the trustee would be unable to sell the entire company through a section 363 sale.

modify those state law duties. This means that trustees of nonprofits or benefit corporations should not necessarily select the highest monetary bid, but they should instead prepare bidding procedures that show how such a sale complies its fiduciary duties: obedience to the mission of the nonprofit or balancing moneymaking against public benefit, as appropriate.[168]

This conclusion is not without precedent. The requirement that the trustee or DIP select the "highest and best offer," though often intoned in bankruptcy cases, is not an ironclad rule. In *Bakalis*,[169] a chapter 7 trustee turned down a higher monetary bid from a competitor in favor of a lower bid without any material contingencies.[170] In a seminal opinion, the court authorized the sale, noting the financial risk of the higher bid and observing as well that the winning buyer would operate the business as a neighborhood institution with minimal disruption.[171] The *Bakalis* court recognized that "[t]he trustee's duty to maximize the return to a bankruptcy estate often does require recommendation of the highest monetary bid."[172] But the court declined to adopt a bright line rule, stating that "a 'highest' bid is not always the 'highest and best' bid."[173]

Similarly, in *160 Royal Palm*, the debtor selected a bid that was $1 million less than the highest monetary bid. The court approved the sale to the lower bidder because the lower bid was a stable and certain offer and the higher

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[168] *See* Hampson, *supra* note 7; *see also In re* Mt. States Rosen, LLC, 619 B.R. 750, 756 (Bankr. D. Wyo. 2020) ("Neither as part of the bid procedures nor the auction process did FAB assert Debtor should give value to its intent to continue operating the facility but now claims it was a mistake for Debtor not to do so. [Although] courts [have] found it appropriate to give value to factors such as continual employment.").

[169] *In re* Bakalis, 220 B.R. 525, 533 (Bankr. E.D.N.Y. 1998).

[170] *Id.* at 531. Charalabos Bakalis owned substantial shares of Olympian Bank, a small neighborhood bank in Queens, and those shares became a part of the chapter 7 bankruptcy estate. *Id.* at 527. If possible, the trustee wanted to obtain a buyer who would continue to operate the bank. *Id.* at 530. During the auction, two buyers distinguished themselves. *Id.* at 529–30. The first was Atlantic, a competitor bank. *Id.* at 530. The second was Holdings, composed of about 50 investors including four Olympian bank officers and directors. *Id.* at 529. Atlantic offered the highest monetary bid at $11.2 million but included significant walk-away provisions which could have jeopardized Olympian's ability to continue operations. *Id.* at 530. The Holdings bid, on the other hand, was structured simply as a stock purchase agreement for $10.5 million without material contingencies. *Id.* at 529. The trustee and his advisors examined the final bids and decided to accept the Holdings bid. *Id.* at 530.

[171] The trustee explicitly included in his analysis "the chance that business disruption might result from a sale to Atlantic, concluding that a possible loss of key management may well be deleterious to the profitable operations of Olympian Bank." *Id.* at 530. The court noted that "Olympian Bank is a small neighborhood institution that relies on personal relationships" and that "a departure of key people may result in loss of deposits and a corresponding diminution of value of the stock." *Id.*

[172] *Id.* at 533.

[173] *Id.*

bidder had previously defaulted in a similar auction.[174] But the court also agreed that the debtor had legitimate concerns that the higher bidder's litigiousness would negatively affect the estate. Maximization of value to the creditors included consideration of finality, stability, and avoidance of litigation for the restructuring debtor, not simply netting another million dollars for the bankruptcy estate. *Bakalis* and *160 Royal Palm* remind us that trustee may have enjoy more latitude for the implementation of values than previously understood.[175]

In light of the trustee's fiduciary duties, I think bankruptcy courts should insist that a trustee attempting a going-concern sale demonstrate to the court's satisfaction that (1) the bidding procedures are consistent with the fiduciary duties of the trustee; (2) the bidding procedures have gained broad support from the estate's beneficiaries; and (3) the sale could not effectively be consummated through a chapter 11 plan.

The counterarguments to such an approach, of course, are not to be brushed aside. A clear rule requiring the trustee to accept the highest monetary bid imposes a certain discipline on a business that may need it. Indeed, the debtor's commitments to public benefit may have been vacuous, ineffective, or corrupt, giving rise to "greenwashing" concerns. Yet the need for discipline goes both ways: debtors may have labored under liability or reputational weight from an overemphasis on profit, and so while bankruptcy court may be an occasion to tighten belts, cut out waste, root out graft, and focus on core business objectives, that does not always mean abandoning the core social commitments of the firm.

Let's imagine that Green Creek could be sold (a) to a "strategic" buyer, like Amazon or UPS, who wants to eliminate competition or (b) to a "financial" buyer, who wants to grow the business. While the strategic buyer offers more cash and can consummate the sale immediately, the financial buyer promises to re-hire the employees, who would otherwise be fired. First, one might worry that selling to the financial buyer is an end run around

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[174] *In re* 160 Royal Palm, LLC, 600 B.R. 119, 129 (S.D. Fla. 2019).

[175] This can be true of bidding procedures too. In *WFDR*, an interested party objected to the auction procedure to sell a radio station, claiming that the DIP's lack of advertising adversely affected the value and quality of submitted bids. *In re* WFDR, Inc., 10 B.R. 109, 110 (Bankr. N.D. Ga. 1981). The DIP disputed this characterization, arguing that "the radio industry [is] a very closely-knit trade group and that word-of-mouth marketing constitutes an appropriate means … to sell this radio station." *Id.* The DIP also pointed out that it was better for the station's current advertising to conduct a word-of-mouth sale, since advertisers would be less willing to buy slots from a radio station for sale. *Id.*

For a discussion of how benefit debtors might build their duty of balancing into section 363 bidding procedures, see Hampson, *supra* note 7, at 140–41; *see also* Gary M. Schildhorn & Brya Keilson, *The Unresolved Dilemma of Creditors' vs. Stakeholders' Rights*, AM. BANKR. INST. J., May 2013, at 86.

the voting and priority rules of the chapter 11 plan process.[176] Of course, the sale documents themselves don't contain any restrictions on what to do with the cash: after the sale, the proceeds will go to secured creditors, then priority creditors, and then *pro rata* to general unsecured creditors. But isn't there a distributive regime hidden in the sale? Although the dollar value of the offer is less, Green Creek's former employees receive more value because of their ability to enter into a business relationship with the financial buyer, which they couldn't do (or wouldn't want to do) with Amazon or UPS.

As a formal matter, though, the employees in our example are not receiving value on account of their prepetition claims; they are receiving value in exchange for their future labor. And that reveals the underlying problem with this argument: it proves far too much. Any sale in bankruptcy puts the assets in the hands of a buyer, and any creditor would benefit from the buyer of their choice taking the assets. Just as employees want the reorganized firm to be a potential employer, financial creditors like banks and hedge funds want the reorganized firm to be a potential borrower.

In any event, such concerns should be addressed by the three-part test that I introduce above. Where a going-concern sale could be consummated through a plan — *i.e.*, through voting — the trustee should use the plan negotiation process.

IV. THE DEBTOR

Next, we turn to the debtor. Naturally, the debtor is insolvent or, at a minimum, financially distressed. That means that under state corporate governance law, the corporation must consider the interests of creditors, rather than shareholders.[177] The mechanism for this shift in fiduciary focus varies by state. In some states, under the trust doctrine, the directors and officers owe fiduciary duties directly to creditors.[178] In Delaware, under *North American Catholic Educational Programming Foundation, Inc. v.*

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[176] This kind of end run is referred to in the bankruptcy doctrine as a "*sub rosa* plan," a sale in bankruptcy that comes with strings attached, strings that make it look like the trustee is trying to get all the distributional effects of a plan without going through the rigor of voting and the confirmation rules in section 1129(a) and (b). *See, e.g.*, *In re* SAS AB, 644 B.R. 267, 271 (Bankr. S.D.N.Y. 2022).

[177] *See, e.g.*, LoPucki & Whitford, *supra* note 90, at 707–08 ("Once insolvency intervenes, it is creditors who will bear the bulk of the company's losses, so they should be able to initiate legal action when losses result from inappropriate management behavior.").

[178] *See, e.g.*, N.Y. Credit Men's Adjustment Bureau, Inc. v. Weiss, 110 N.E.2d 397, 398 (N.Y. 1953) ("If the corporation was insolvent at that time it is clear that defendants, as officers and directors thereof, were to be considered as though trustees of the property for the corporate creditor-beneficiaries.").

Gheewalla,[179] creditors obtain derivative standing to bring fiduciary duty claims against the directors and officers.[180]

Even so, for nonprofit corporations and benefit corporations, the duties of obedience and balancing do not vanish upon insolvency. The legislative history of the benefit corporation statute makes clear that directors must balance public benefit and money-making even in change-of-control situations.[181]

In a bankruptcy case, a debtor has certain duties regardless of whether a separate trustee has been appointed, such as filing a list of creditors, a schedule of assets and liabilities, and a statement of its financial affairs.[182] Whether it has any other statutory or fiduciary duties depends on whether it has taken on the role of debtor in possession. In this part, I map out those fiduciary obligations and explore how they interrelate, especially when the debtor steps into the trustee's shoes to manage and operate the estate.

A. The Debtor on the Eve of Bankruptcy

On the eve of bankruptcy, the debtor's fiduciary duties come from state law. Upon insolvency, those fiduciary duties require special consideration to creditors when deciding whether to file.[183] The directors and officers of nonprofit and benefit corporations must reconcile their duties of obedience and balancing with their condition of insolvency.

In recent years, some creditors have sought, as a condition of rescue financing, overriding decisionmaking authority over the decision whether to file for bankruptcy, through either (a) a "golden share," a share that entitles its holder to vote or veto a bankruptcy filing, or (b) a "golden director," a likeminded individual who may vote or veto a bankruptcy filing. Courts are currently grappling with the effectiveness of such provisions, which are clear

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[179] 930 A.2d 92 (Del. 2007).

[180] *Id.* at 101. To Hu and Westbrook, this duty shifting upon insolvency is a poor fit for state corporate governance law, and they urge state courts to abolish the doctrine — allowing bankruptcy law (and *only* bankruptcy law) to create fiduciary duties to creditors. Hu & Westbrook, *supra* note 128.

[181] *See, e.g.*, Hampson, *supra* note 7, at 115 (noting that the benefit corporation legislation provides that directors and officers meet their fiduciary obligations when they are disinterested, reasonably informed, acting in good faith, and balancing public benefit); *see also* FREDERICK H. ALEXANDER, PURSUING PROFIT WITH PURPOSE: BENEFIT CORPORATION LAW AND GOVERNANCE 123–26 (2018).

[182] 11 U.S.C. § 521(a)(1). Debtors also receive certain benefits, like exemptions under section 522, that apply in individual cases.

[183] For all debtors, however, attempts to waive or delegate the decision whether to file bankruptcy are unlikely to succeed. Bankruptcy courts have held that debtors may not waive the right to file bankruptcy.

attempts to skirt the rule against waivers of bankruptcy filings.[184]

Similarly, debtors frequently strike bargains with creditors about the shape and trajectory of a bankruptcy case. Such debtors, alongside secured creditors, may agree on financing in advance, or even on a plan of reorganization — locking in groups of supporting creditors in a restructuring support agreement ("RSA") or plan support agreement ("PSA"). Those arrangements, too, are subject to preexisting, state law fiduciary obligations. In binding the firm to a certain course of action, directors must comply with their fiduciary duties. In some instances, directors insist on a "fiduciary out," a contractual escape clause that allows them to renegotiate the deal if a court finds that entering into it violated their fiduciary duties in the first place.[185]

B. The Debtor in Possession

Once the debtor has filed for bankruptcy, in most chapter 11 cases, the estate may be managed and operated by the debtor itself, wearing the cap of the trustee. The debtor in possession (or "DIP") is a distinctly American innovation, now exported around the world.[186] One might wonder whether the same group of directors that brought the company into bankruptcy should be entrusted with its care while in bankruptcy, and indeed over the long arc of American bankruptcy practice, the default has flipped back and forth twice.[187] But the Code has a mechanism for displacing those directors,[188] and contemporary insolvency practice is to appoint some new "bankruptcy directors" to provide a professional and independent perspective on the board.[189]

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[184] Indeed, even if golden shares and golden directors are effective, the people holding the power likely take with it fiduciary obligations to the debtor. A precipitous bankruptcy filing, or a pigheaded refusal to file — especially where such decisions trigger concerns about the duty of loyalty — will expose golden shareholders and golden directors to liability for breach of fiduciary duty.

[185] *See* Edward J. Janger & Adam Levitin, *Badges of Opportunism: Principles for Policing Restructuring Support Agreements*, 13 BROOKLYN J. CORP. FIN. & COM. L. 169, 173 (2020).

[186] *See supra* note 5.

[187] *See, e.g.*, JEREMIAH D. LAMBERT & GEOFFREY S. STEWART, THE ANOINTED 89–90, 92–93 (2021) (describing the role of old management in the equity receivership and the New Deal dispossession, championed by William O. Douglas, in the Chandler Act of 1938).

[188] *See infra* notes __-__ and accompanying text.

[189] *See, e.g.*, John Wm. ("Jack") Butler, Jr. et al., *Preserving State Corporate Governance Law in Chapter 11: Maximizing Value Through Traditional Fiduciaries*, 18 AM. BANKR. INST. L. REV. 337, 341–52 (2010) (explaining that the immense power of a DIP must be checked by a series of oversight mechanisms to prevent dishonest or grossly incompetent management). For example, in his "First Day Declaration" in the bankruptcy of FTX, the

Courts and commentators agree that the DIP (and its officers and directors) takes on both the statutory and the fiduciary duties of the trustee.[190] As with fiduciary duties generally, the Code does not set forth this result expressly, but courts have read it in.[191] Indeed, Congress seemed to contemplate this result when it passed the Code in 1978.[192] These fiduciary duties have given rise to knotty questions about the DIP's corporate governance, such as whether shareholders can replace the board during

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cryptocurrency exchange that collapsed in 2022, new CEO John Jay Ray III lambasted the company's prior corporate governance, saying that he had never seen "such a complete failure of corporate control." David Yaffe-Bellany, *New Chief Calls FTX's Corporate Control a "Complete Failure,"* N.Y. TIMES (Nov. 17, 2022), www.nytimes.com/2022/11/17/business/ftx-bankruptcy.html. Still, the independence of such directors has been recently challenged. *See* Jared A. Ellias, Ehud Kamar & Kobi Kastiel, *The Rise of Bankruptcy Directors*, 95 S. CAL. L. REV. 1083 (2022) (questioning the independence of bankruptcy directors drawn from a small pool of repeat players).

[190] *See* CFTC v. Weintraub, 471 U.S. 343, 355 (1985) (quoting Wolf v. Weinstein, 372 U.S. 633, 651 (1963)) ("[T]he willingness of courts to leave debtors in possession is premised upon an assurance that the officers and managing employees can be depended upon to carry out the fiduciary duties of a trustee."); s*ee also In re* Johns-Manville Corp., 60 B.R. 612 (Bankr. S.D.N.Y. 1986); Weinstein, 372 U.S. at 649–50; Weintraub, 471 U.S. at 355 ("If a debtor remains in possession, the debtor's directors have essentially the same fiduciary obligations to creditors and shareholders as would the trustee for a debtor out of possession.").

At one point, some courts had opined that the DIP was a separate entity from the debtor, generating significant confusion. *See, e.g.*, *In re* Brent Expls., Inc., 31 B.R. 745, 752 (Bankr. D. Colo. 1983), Kelch, *supra* note 99, at 1330–34. The Supreme Court has rejected that view. *See* NLRB v. Bildisco & Bildisco, 465 U.S. 513, 528 (1984) ("Obviously if the [DIP] were a wholly 'new entity,' it would be unnecessary for the Bankruptcy Code to allow it to reject executory contracts, since it would not be bound by such contracts in the first place. For our purposes, it is sensible to view the debtor-in-possession as the same 'entity' which existed before the filing of the bankruptcy petition, but empowered by virtue of the Bankruptcy Code to deal with its contracts and property in a manner it could not have done absent the bankruptcy filing."). The Supreme Court's reasoning was flawed, though, since it is the *trustee* who is empowered to reject executory contracts, not (in the first instance) the DIP. *See* 11 U.S.C. § 365(a). Indeed, it is only because the DIP is the same entity as the debtor that we see a tortured splintering of perspectives on whether the trustee or DIP may assume a personal services contract even if it could not assign it under nonbankruptcy law. *See* 11 U.S.C. § 365(c)(1).

[191] *See, e.g.*, *In re Count Liberty, LLC*, 370 B.R. 259, 280 (Bankr. C.D. Cal. 2007) (collecting cases).

[192] H.R. Rep. No. 95-595, at 404 (1977) ("This section [§ 1107(a)] places a debtor-in-possession in the shoes of a trustee in every way. The debtor is given the rights and powers of a chapter 11 trustee. He is required to perform the functions and duties of a chapter 11 trustee (except the investigative duties). He is also subject to any limitations on a chapter 11 trustee, and to such other limitations and conditions as the court prescribes."); *see also* S. Rep. No. 95-989, 95th Cong., 2d Sess., at 118 (1978) (same).

bankruptcy[193] or whether the DIP acts at cross-purposes with its duties by proposing a plan.[194]

But once we carefully parse the fiduciary duties of the trustee and the fiduciary duties of the debtor, we can see the solution clearly: the DIP has two sets of fiduciary duties.[195] What is called for is greater reflection on the nature and scope of these stacked fiduciary duties. I thus join Lubben in calling for bankruptcy debtors to take their DIP duties seriously, including — as he proposes — by reassessing any restructuring support agreement and DIP financing upon a filing in bankruptcy.[196]

This may lead some corporate counsel to wonder whether all debtors can serve as DIPs. Can a nonprofit or benefit debtor, like Green Creek, take on DIP duties without violating its duties of balancing or obedience? I think so.[197] I see plenty of room for interpretation on both fronts, especially once we realize that the creditor body is often *closer* to the missions of nonprofits and benefit corporations than the shareholder body.[198] Thus, nonprofit or benefit debtors can comply with a fiduciary "duty to clear runway" while

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[193] Whether a bankruptcy court steps in to prevent shareholders from exercising their corporate governance authority turns on whether the proposed changes interfere with the prospect of reorganization. *See, e.g.*, Skeel, *supra* note 91, at 507–09; Beinenstock, *supra* note 133, at 554; Bogart, *supra* note 18, at 158; Frost, *supra* note 19, at 113–115 (discussing the court's role in preventing corporate managers in the Johns-Manville Corporation from "scuttl[ing]" the development of a bankruptcy plan); *see also* Miller, *supra* note 90, at 1491 ("Chapter 11 of the Bankruptcy Code is devoid of any indication that stockholders of an insolvent corporation are stripped of corporate governance rights available under applicable nonbankruptcy law absent a direct conflict with the bankruptcy law.").

[194] Bogart adverts to some scholarly debate about "[t]he fact that the DIP always has a self-interest in the development of the plan of reorganization leads many scholars to the incorrect conclusion that the DIP acts in a disloyal manner and therefore violates its fiduciary obligations merely by negotiating the plan." Bogart¸ *supra* note 18, at 214. Any such debate would have to take account of the fact that the *debtor*, not the trustee, has the exclusive right to file a plan in chapter 11. *See* 11 U.S.C. § 1121(b).

[195] *See, e.g.*, Miller, *supra* note 90, at 1468; Nimmer & Feinberg, *supra* note 20, at 32 ("Bankruptcy does not eradicate prior obligations stemming from the debtor's business structure. It merely adds the quasi-trustee obligations of a DIP").

[196] *See* Lubben, *supra* note 46, at 36–47 (advancing an "applied account of DIP fiduciary duties); *see also* Edward J. Janger & Adam Levitin, *Badges of Opportunism: Principles for Policing Restructuring Support Agreements*, 13 BROOKLYN J. CORP. FIN. & COM. L. 169 (2020).

[197] Of course, to the extent that corporate counsel concluded that they could not, they could simply move for the appointment of a chapter 11 trustee. The fact that debtors almost never seek appointment of a trustee themselves may indicate that debtors and their boards believe that they can comply with both sets of duties. This does not, of course, mean that they always will. Nimmer and Feinberg point out that owners of closely held companies need to reframe their understanding of their business: it "is no longer a personal preserve responding only to the interests of the owner." Nimmer & Feinberg, *supra* note 20, at 41.

[198] *See, e.g.*, LoPucki, *supra* note 127.

simultaneously proposing a plan that attempts to save the life of the debtor company. And, crucially, the power to propose a plan is, in the first instance, a power of the *debtor*.[199]

What about asset sales under section 363? As discussed above, despite the Code's clear focus on plans, many chapter 11 plans effectively terminate after a sale. Technically speaking, the power to sell under section 363 is a power of the *trustee*,[200] and so when the DIP undertakes such a sale, it must comply with both sets of fiduciary duties. If the duty to facilitate theory is correct, that means that 363 sales should not be used to truncate plan negotiation process. Indeed, since 363 sales can be part of a bankruptcy plan,[201] debtors should conduct such sales as part of a plan instead of conducting them as freestanding sales. This approach runs against the grain of contemporary chapter 11 practice, as section 363 has become a common "exit strategy" for reorganization cases.[202]

C. The Debtor Dispossessed

While DIP operation of the estate is the default in chapter 11 cases, the debtor can be dislodged from its position as DIP through a motion for the appointment of a chapter 11 trustee or a motion to convert the case to chapter 7. The court can order a trustee appointed for a fairly low bar, the "interests of creditors," though more commonly trustees are appointed for "fraud, dishonesty, incompetence, or gross mismanagement of the affairs of the debtor."[203] Indeed, some courts have appointed a chapter 11 trustee based upon a breach of fiduciary duties to creditors.[204] And (so long as the debtor

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[199] 11 U.S.C. § 1121(b).

[200] *Compare* 11 U.S.C. § 363(b)(1), *with id.* § 1121(b); *see also* Miller, *supra* note 90, at 1491 ("The Bankruptcy Code contemplates that, initially at least, the debtor will lead the plan formulation process."). Still, section 363 also requires that the trustee use, sell, or lease property from the estates of nonprofit property "only in accordance with nonbankruptcy law applicable to the transfer of property by [such] a debtor." 11 U.S.C. § 363(d). That provision tightens the scope of the trustee's authority over the estate of a nonprofit debtor and therefore reduces any difference between what the fiduciary duties might otherwise allow.

[201] 11 U.S.C. §§ 1123(a)(5)(D); (b)(4).

[202] *See, e.g.*, Douglas G. Baird & Robert K. Rasmussen, *The End of Bankruptcy*, 55 STAN. L. REV. 751, 751–53 (2002); ELIZABETH WARREN ET AL., THE LAW OF DEBTORS AND CREDITORS: TEXT, CASES, AND PROBLEMS 679 (8th ed. 2021).

[203] 11 U.S.C. § 1104(a).

[204] *See* Bienenstock, *supra* note 133, at 551 (quoting *In re V. Savino Oil & Heating Co.*, 99 B.R. 518 (Bankr. E.D.N.Y. 1989)).

is not a nonprofit[205]), the court can convert a case to a chapter 7 liquidation for "cause," when it is in the "best interests of creditors and the estate."[206]

Once the debtor has been dispossessed of the estate, its fiduciary duties revert to its pre-bankruptcy state; it no longer owes fiduciary duties as the trustee. That said, the debtor dispossessed also has fewer powers under the Code. The debtor's once-unilateral right to convert a case to chapter 7 vanishes,[207] as well as its exclusive right to file a plan.[208]

V. THE CREDITORS

Lastly, we turn to the creditors. We are used to thinking of creditors as wanting to be repaid in full — and, in bankruptcy, to be repaid as many cents on the dollar as possible. Yet consider the many situations where creditors may care about more than monetary distribution alone. Employees and trade vendors may want a business to survive for the resilience of the local economy. Socially responsible investment firms might be willing to take a haircut to help an otherwise viable company recover. Even tort victims may want more than just money: consider, for example, the tort victims in the Catholic diocese cases. While monetary compensation is important, so too is an acknowledgment of responsibility and commitment to change.

The fiduciary duties of creditors may seem more straightforward than for the trustee or the debtor: after all, creditors do not manage or operate the estate. Yet creditors, too, may have "stacked" fiduciary duties when they take on extra roles in a bankruptcy case. These sets of fiduciary duties must be thoughtfully analyzed too, particularly when the creditor body includes nonprofits, benefit corporations, and other types of social enterprises.

A. Committee Members

First, creditors may owe fiduciary duties to other creditors because they

[205] The court may not convert a case to a liquidation for a debtor that is not a "moneyed, business, or commercial corporation," a standard that encompasses nonprofit corporations. *See* 11 U.S.C. § 1112(c).

[206] 11 U.S.C. § 1112(b)(1). "Cause," as defined in the Code, can include anything from economic problems, like a sharp diminution in the estate's value or the debtor's inability to confirm a plan, to governance problems, like "gross mismanagement of the estate" or failure to comply with mandatory reporting requirements. *See id.* § 1112(b)(4).

[207] *Id.* § 1112(a)(1).

[208] *See id.* § 1121(c)(1) (providing that any party in interest may file a plan when a trustee is appointed). The major exception is in subchapter V, where only the debtor may file a plan — even if a chapter 11 trustee is appointed, dispossessing the small business DIP. 11 U.S.C. § 1189(a). Subchapter V practitioners have flagged this rule as a potential problem worth fixing in the next iteration of the statute.

serve on a committee in a chapter 11 case. Bankruptcy committees come in two types, official (or statutory) committees and *ad hoc* committees. The Code provides for the appointment of one statutory committee of unsecured creditors and allows for the appointment of additional statutory committees on an as-needed basis.[209] *Ad hoc* committees, by contrast, are self-organized, but must disclose their membership regularly on the docket.[210]

The two types of committees differ in two main ways. The expenses of official committees are paid out of the estate,[211] and official committees receive inside information from the trustee or debtor, while *ad hoc* committees have no right to such payment or information.[212] Indeed, since this information may consitute material nonpublic information ("MNPI") for purposes of insider trading laws, creditors who wish to preserve their ability to trade sometimes decline to serve on official committees.

Throughout the duration of the case, official committees consult with the trustee or debtor, investigate the debtor, participate in plan negotiation, and advocate in other ways for the "interest of those represented."[213] Official committees are required to listen to and share information with the creditors they represent.[214] *Ad hoc* committees, while not statutorily charged with that role, undertake much the same kind of endeavor on behalf of their constituents.[215]

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[209] The official committee of unsecured creditors is appointed by the U.S. Trustee's Office and is ordinarily composed of the top seven largest claimholders (of those willing to serve). Sometimes creditors form committees prior to the filing of a bankruptcy case, and the U.S. Trustee's Office can endorse such committees, so long as the membership was "fairly chosen" and "representative." 11 U.S.C. § 1102(b)(1). A similar approach is used for equity security holders. *Id.* A bankruptcy court might appoint a committee of equity security holders "if necessary to assure adequate representation of creditors or of equity security holders." 11 U.S.C. § 1102(a)(2). In practice, equity committees are rarely appointed, because an enterprise deep in insolvency has nothing left to pay equity at the end of the case: all the value goes to creditors. Most courts require that there must be a "substantial likelihood of a meaningful distribution" to equity security holders before they will consider appointing an equity committee. *See, e.g.*, *In re Celsius Network LLC*, 645 B.R. 165, 174 (Bankr. S.D.N.Y. 2022).

[210] *See* Fed. R. Bankr. P. 2019.

[211] 11 U.S.C. § 1103(a); *see also* Diane Lourdes Dick, *Grassroots Shareholder Activism in Large Commercial Bankruptcies*, 40 J. CORP. L. 1, 8 (2014).

[212] *See, e.g.*, Michelle M. Harner & Jamie Marincic, *Committee Capture — An Empirical Analysis of the Role of Creditors' Committees in Business Reorganizations*, 64 VAND. L. REV. 747, 810 (2011).

[213] 11 U.S.C. § 1103(c).

[214] *See id.* § 1102(b)(3).

[215] The impact that committees have on the pace and outcome of bankruptcy cases is complex. Then-Professor (now-Judge) Michelle Harner and quantitative researcher Jamie Marincic found in a 2011 empirical study that cases with a single creditors' committee were

As official representatives of a class of creditors, members of official committees owe fiduciary duties to that class. As before, the Code does not say so expressly, but courts are uniform in their understanding that the statutory provisions generate a fiduciary relationship. Courts take those duties seriously. During the *Neiman Marcus* bankruptcy, attorney and hedge fund founder Dan Kamensky sat on the official committee while his firm Marble Ridge Capital was bidding on Neiman Marcus assets. In breach of his fiduciary duties, Kamensky pressured a rival bidder to abandon its bid so that Marble Ridge could obtain the assets at an artificially lower price — a move that helped Marble Ridge but undercut the creditors who were hoping for the auction to yield as high a price as possible. Among other consequences, Kamensky eventually pled guilty to bankruptcy fraud.[216]

Where the committee member is an individual, the analysis ends there. But where the committee member is a business organization, it owes a separate set of fiduciary duties under nonbankruptcy law and thus has stacked fiduciary duties, just like a DIP. Committee membership does not excuse a committee member from complying with its preexisting, state law fiduciary duties.

This raises tough questions in an era of clashing norms. Imagine creditors that are themselves nonprofit or benefit corporations, bound by their fiduciary duties to approach the bankruptcy case in light of their corporate purpose. What if such creditors do not want to maximize the dollar value of their distribution over all other outcomes? What if they want the estate to be operated according to CSR or ESG values?

The U.S. Trustee's Office should weigh such constituencies seriously when selecting committee members. The statute's preference for the creditors holding the largest claims is just the "ordinary" rule, and creditors may ask the court to depart from it when "necessary to ensure adequate representation of creditors or equity security holders."[217] For its part, a nonprofit or benefit creditor should seek a committee seat only when it

more likely to result in a liquidation or sale, as compared to a plan, and were also more likely to pay unsecured creditors fifty cents on the dollar or less. Harner & Marincic, *supra* note 212 at 755. For a more fulsome discussion of Harner and Marincic's findings, see *id.* at 795–99 (proposing an "increased focus on committee composition, use of multiple committees, and increased public disclosures"). Harner previously described persistent problems with conflicts of interest among bankruptcy fiduciaries and proposed a "case facilitator," which resembles the facilitating role of the subchapter V trustee. *See* Michelle M. Harner, *The Search for an Unbiased Fiduciary in Corporate Reorganizations*, 86 NOTRE DAME L. REV. 469, 508–22 (2011).

[216] *See, e.g.*, King & Spalding, *Neiman Marcus and the Fiduciary Duties of Creditors' Committee Members* (June 29, 2021), https://www.jdsupra.com/legalnews/neiman-marcus-and-the-fiduciary-duties-2693615/.

[217] *Id.* § 1102(a)(2).

concludes that it represents a significant constituency within the class of creditors. Otherwise, its nonbankruptcy fiduciary duties would clash with its committee fiduciary duties. If such a constituency exists, however, a creditor does not breach its fiduciary duty by voting accordingly: indeed, the odd number of committee members suggests that majority rule is an appropriate way to avoid deadlock. Still, to avoid any appearance of impropriety, the committee should solicit the views of its constituency before making major decisions about the committee's position at key junctures in the case.[218]

Alternatively, the U.S. Trustee's Office could, in appropriate cases, appoint a separate committee to represent nonprofit or benefit creditors.[219] We might call it a "benefit committee." Such a committee could, like an official committee, retain counsel, seek discovery, and attempt through negotiation and advocacy to influence the course of the case. Where concerns about conflicts of interest threaten to ennervate the advocacy of nonprofit or benefit creditors, a benefit committee could be an elegant solution.

To succeed, such constituencies must be unwavering in their commitment to social values. Committee work in bankruptcy is fast-paced; committees form in the early days of a bankruptcy case and must learn the ropes of the case quickly.[220] And not every bankruptcy of a social enterprise will be negotiated alongside likeminded creditors: by the time a bankruptcy petition has been filed, those creditors may have already traded out of their position, allowing distressed-debt investors (who may not share those same norms) to take their place.

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[218] *See* 11 U.S.C. § 1102(b)(3)(B) (authorizing a committee to "solicit and receive comments from" its constituency).

[219] *See id.* § 1102(a)(2) (allowing a court to "order the appointment of additional committees of creditors or of equity security holders if necessary to assure adequate representation of creditors or of equity security holders"). This approach is consistent with the proposals advanced by Harner and Marincic. *See* Harner & Marincic, *supra* note 212, at 799. Stephen H. Case suggested that management announce a pro-equity stance, a pro-creditor stance, or a stakeholder-mediator stance early in a bankruptcy case. Constituencies not represented by management would then seek representation by a committee funded out of the estate. Stephen H. Case, *Fiduciary Duty of Corporate Directors and Officers, Resolution of Conflicts Between Creditors and Shareholders, and Removal of Directors by Dissident Shareholders in Chapter 11 Cases*, in ALI-ABA COMM. ON CONTINUING PROFESSIONAL EDUC., THE WILLIAMSBURG CONFERENCE ON BANKRUPTCY: CRITIQUE OF THE FIRST DECADE UNDER THE BANKRUPTCY CODE AND AGENDA FOR REFORM 373, 382–85 (1988). LoPucki and Whitford criticize this proposal as simply deferring all the thorny governance questions to the court, which would have to adjudicate any disputes. *See* LoPucki & Whitford, *supra* note 90, at 779.

[220] Bankruptcy committees get started later than the debtor and the DIP and must learn the case at breakneck speed in the fast-paced context of Chapter 11. *See* Miller, *supra* note __, at *12–13; *see also* Jonathan C. Lipson, *Bargaining Bankrupt: A Relational Theory of Contract in Bankruptcy*, 6 HARV. BUS. L. REV. 239, 255 (2016).

B. DIP Lenders

Second, individual creditors may owe fiduciary duties to the bankruptcy estate if they exercise extraordinary control over its decisionmaking. This relationship (and accompanying risk) is rare, and rightly so, but as DIP lenders exercise more and more control over the course of bankruptcy estates, courts may wish to sketch out the limits on the control DIP lenders can exert without taking on fiduciary obligations.

As discussed above, fiduciary duties arise in principal-agent relationships, or when someone controls the property of another.[221] Typically, of course, the creditor-debtor relationship is an arms'-length one. Even strict covenants and conditions in a loan agreement are insufficient to give rise to fiduciary duties. That said, in recent decades, lenders have exerted a tighter and tighter grip on bankruptcy cases. Debtor companies often find themselves unable to finance their own chapter 11 case. Strapped for cash, they turn to debtor-in-possession lenders for new money, called a DIP loan or DIP financing. Recognizing the inherent difficulty of paying for a bankruptcy case with credit, the Bankruptcy Code authorizes the court to approve new loan facilities with superpriority and priming liens on the debtors' assets.[222]

Yet DIP lenders frequently go far beyond that, seeking to manage the pace and direction of a bankruptcy case through case milestones and "drop dead" dates — covenants and conditions expressly set forth in the deal documents that, if unmet, shut down the line of financing and, with it, the case. DIP lenders have also taken over some of the functions which had traditionally belonged to the bankruptcy court, such as "setting the timeline for filing a plan … setting timetables for the disposition of specific assets; requiring DIP lender approval of auction procedures … and requiring the debtor to waive the estate's preference claims, fraudulent transfer claims, and avoidance powers."[223] They have tried other creative measures too, such as "supervising the implementation of capital improvements; setting prices for the sale of debtor assets; requiring the debtor to hire a new CEO or CRO, subject to the DIP lender's approval; and requiring the debtor to replace existing service providers, such as marketing companies, with lender-approved service providers."[224]

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[221] *See supra* note __ and accompanying text. In corporate law, fiduciaries include not only the corporation and its officers and directors, but also groups of shareholders that effectively control the firm. *In re* Pattern Energy Grp. Inc., 2021 Del. Ch. LEXIS 90, at *96–97, 106 (Del. Ch. 2021).

[222] 11 U.S.C. § 364.

[223] *Id*. at 20.

[224] Phelan, *The Use of Dip Financing* at 19.

Scholars have noted the trend toward increasing DIP lender control with mixed views.[225] Some commentators argue that lender control undermines important goals of Chapter 11 like preservation of value in the form of jobs and continuing operation, especially when lenders are incentivized to extract value from the debtor.[226] Others argue that the high level of Chapter 11 liquidations is attributable to market-driven phenomena rather than lender coercion.[227]

The two most common checks on DIP power seem toothless. As discussed above, the debtor (or trustee) should reconsider the DIP agreement after filing and reject it if it is not in the best interests of the estate.[228] Or the court itself might reject the financing.[229] However, if there is only one offer on the table, both the debtor and the court may hesitate to reject it outright, settling instead for negotiating out any severe or draconian terms

What about imposing fiduciary duties on DIP lenders? To be sure, a lender merely taking the Code-prescribed "sweeteners"[230] is not nearly enough control to establish a fiduciary relationship: Congress envisioned that superpriority and priming liens might be necessary to finance bankruptcy cases, and it did so without a glimmer that such lenders might become fiduciaries. But where the DIP facility gives the lender power akin to "operating the decision-making machinery" of the estate[231] — especially where such control would give rise to a fiduciary relationship outside bankruptcy[232] — the conclusion seems ineluctable. As Professor Tomer Stein has thoughtfully analyzed, creditor control can sometimes give rise to

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[225] See Robin Phelan & Ocean Tama, *The Use of DIP Financing as a Mechanism to Control the Corporate Restructuring Process*, 44 TEX. J. BUS. L. 15 (2011) (describing different loan terms and covenants). Douglas G. Baird & Robert K. Rasmussen, *Private Debt and the Missing Lever of Corporate Governance*, 154 U. PA. L. REV. 1209, 1212 (2006) ("When a business enters financial distress, the major decisions — whether the CEO should go, whether the business should search for a suitor, whether the corporation should file for Chapter 11 — require the blessing of banks.").

[226] Indeed, the DIP lender may have a greater incentive to force the debtor to liquidate assets because of the lender's priority status. *See, e.g.*, David A. Skeel Jr., *The Past, Present and Future of Debtor-in-Possession Financing*, 25 CARDOZO L. REV. 1905, 1907 (2004). When drop dead provisions require liquidation or a fire sale of assets, this may create a conflicted transaction. *See* Lynn M. LoPucki & Joseph W. Doherty, *Bankruptcy Fire Sales*, 106 MICH. L. REV. 1, 26 (2007) (concluding a debtor will receive a lower price if the sale is made earlier in the bankruptcy process).

[227] *Id.* at 24.

[228] *See supra* note 196 and accompanying text.

[229] Frederick Tung, *Financing Failure: Bankruptcy Lending, Credit Market Conditions, and the Financial Crisis*, 37 YALE J. ON REG. 651, 655–58 (2020).

[230] 11 U.S.C. § 364.

[231] *In re* Pattern Energy Grp. Inc., 2021 Del. Ch. LEXIS 90, at *113 (Del. Ch. 2021).

[232] Douglas G. Baird & Robert K. Rasmussen, Private Debt and the Missing Lever of Corporate Governance, 154 U. PA. L. REV. 1209, 1212 (2006).

fiduciary duties."[233]

To my mind, though, the degree of control required to give rise to DIP fiduciary duties must go beyond the strict consequences set forth in contemporary DIP financing documents. (Indeed, those consequences are desperately needed to unlock DIP financing in the first place, and it would be bad policy to disincentivize them.) But where a DIP lender effectively controls the debtor, through board observers or voting members — or where the "milestones" look more like yardsticks — courts should entertain the argument.

What then? Let's imagine a DIP lender in Green Creek's chapter 11 case took or controlled a majority of seats on the Green Creek's board. Like the DIP, the DIP lender would also owe fiduciary duties to the estate, including the duty to facilitate a plan and any state law duties that apply under section 959. Forcing the estate into a fire sale under section 363 would thus constitute a breach of fiduciary duty. To avoid such a result, lenders interested in financing bankruptcy cases should protect themselves through the DIP financing documents and avoid any temptation to exert total control in the bankruptcy boardroom.

VI. STACKED FIDUCIARY DUTIES

To take stock, the landscape of bankruptcy fiduciaries is as follows: The trustee in bankruptcy owes fiduciary duties to the estate and its beneficiaries, and while the source and nature of those duties is unclear, I argue that the trustee has a duty to facilitate the development of a plan, or a "duty to clear runway," and is required to follow state law fiduciary duties in the case of business bankruptcies under 28 U.S.C. § 959. The debtor has its own fiduciary duties under state law and takes up the trustee's fiduciary duties, too, when it takes on the role of DIP. Members of official committees owe their own fiduciary duties under state law and take on additional fiduciary duties to the creditor (or equity shareholder) constituency that they represent on official committees. Some creditors may undertake a fiduciary relationship when they exercise extraordinary control over the decisionmaking of the estate.

This window onto bankruptcy law has implications for bankruptcy theory. It both stirs up old debates and might start some new ones.

A. Stirring Up Old Debates

One of the most prominent bankruptcy debates since the 1978 passage of

[233] Tomer S. Stein, *Debt as Corporate Governance*, 74 HASTINGS L.J. 1281, 1296 (2023).

the Bankruptcy Code focuses on the entitlements that debtors obtain by virtue of seeking bankruptcy protection.

One school of thought is championed by then-Professor and now-Senator Elizabeth Warren. Sometimes called "traditionalists" or "functionalists," this camp views the bankruptcy courts as implementing Congressional policy. I prefer to call this camp the "institutionalists," because the underlying notion, it seems to me, is that federal institutions are entitled to carry out federal policy. That means that Congress can take affirmative steps to protect debtor companies, and can exalt creditors or make them low as it sees fit.[234]

By contrast, the "proceduralists," championed by Professors Thomas H. Jackson, Douglas Baird and others, see bankruptcy as a federal forum for managing financial distress.[235] Protections like the automatic stay are not seen as substantive but as procedural necessities to allow a bargaining process to be implemented.[236] Bankruptcy should implement nonbankruptcy entitlements as closely as possible, to avoid any incentives for debtors to forum-shop into federal court.[237] The bankruptcy system, therefore, should resemble something like a hypothetical "Creditors' Bargain" — what the creditors would have negotiated for *ex ante*.

The whole arena of bankruptcy fiduciaries muddies the waters. One would expect institutionalists like Warren to support a clear, federal fiduciary duty, rather than allowing state-law fiduciary duties to persist into bankruptcy. Yet no federal duty of obedience or balancing exists, so a federal rule is less protective of community welfare than a state one, at least for some debtors.[238] Indeed, the content of the federal fiduciary duty, at least in

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[234] *See, e.g.*, Ronald Mann, *Bankruptcy and the Entitlements of the Government: Whose Money Is It Anyway?*, 70 N.Y.U. L. REV. 993 (1995).

[235] The debate between the institutionalists and the proceduralists hit a high point in the 1980s, with a series of back-and-forth law review articles. *See, e.g.*, Elizabeth Warren, *Bankruptcy Policymaking in an Imperfect World*, 92 MICH. L. REV. 336 (1993); Douglas G. Baird, *Loss Distribution, Forum Shopping, and Bankruptcy: a Reply to Warren*, 54 U. CHI. L. REV. 815 (1987); Elizabeth Warren, *Bankruptcy Policy*, 54 U. CHI. L. REV. 775 (1978); *see also* Douglas G. Baird & Thomas H. Jackson, *Fraudulent Conveyance Law and Its Proper* Domain, 38 VAND. L. REV. 829 (1985); Thomas H. Jackson, *Bankruptcy, Non-Bankruptcy Entitlements, and the Creditors' Bargain*, 91 YALE L.J. 857, 860 (1982). Although Baird previously declared an impasse, *see* Douglas G. Baird, *Bankruptcy's Uncontested Axioms*, 108 YALE L.J. 573 (1998), most recently he appears to have declared victory. *See* BAIRD, *supra* note 16, at 184 (claiming that the proceduralist "view of reorganization law does not seem especially controversial today).

[236] *See, e.g.*, BAIRD, *supra* note 16, at 108.

[237] *See, e.g.*, Douglas G. Baird, *Loss Distribution, Forum Shopping, and Bankruptcy: A Reply to Warren*, 54 U. CHI. L. REV. 815, 828 (1987) ("Allowing priorities outside of bankruptcy but not inside is an open invitation to forum shopping and would exacerbate all the problems Jackson and I want to minimize").

[238] *See, e.g.*, Donald R. Korobkin, *Rehabilitating Values: A Jurisprudence of*

reorganization cases, is quintessentially procedural — the duty to facilitate a plan or the duty to "clear runway."

By contrast, proceduralists ought to support the idea that the trustee in bankruptcy should operate the estate under the same fiduciary obligations that the officers and directors would have under state law.[239] Otherwise, we would create a perverse incentive for debtors to "shed" their nonprofit or benefit corporation status by filing for bankruptcy.[240] Yet those state law duties, incorporated by section 959, represent a real substantive change from what most people imagine the Creditors' Bargain to be.

The closest vision to what I am advocating here is LoPucki's application of team production theory to bankruptcy. Drawing from Professors Margaret Blair and Lynn Stout, LoPucki argued that the governance of insolvent corporations in bankruptcy should encompass the interests of stakeholders.[241] That view of bankruptcy decisionmaking approximates the mission-oriented fiduciary duties of nonprofits and benefit corporations, but the duties of obedience and balancing would put an even finer edge on things.

To be fair, I do not know for sure how exactly battle lines would be drawn in a new round of this debate. The questions I am posing do not strike me as having easy answers. But they do introduce a new front, as it were, in the substantive/procedural theatre.

Bankruptcy, 91 COLUM. L. REV. 717, 732–39 (1991); Robert E. Scott, *Through Bankruptcy With the Creditors' Bargain Heuristic*, 53 U. CHI. L. REV. 690, 700–08 (1986); Elizabeth Warren, *Bankruptcy Policy*, 54 U. CHI. L. REV. 775, 777, 802–083 (1987).

[239] In 1992, as chapter 11 was facing heavy criticism, Skeel argued that the states would do better at corporate governance questions in an insolvency process, citing arguments that sound in federalism, state-level innovation and competition, historic strengths and expertise at the state level. *See* Skeel, *supra* note 91, at 513-26.

[240] Indeed, maintaining the same fiduciary obligations inside bankruptcy as outside is reminiscent of Professor Robert Rasmussen's idea of "menu" bankruptcy, where debtors and creditors could agree on the insolvency regime that would govern in the case of financial distress, though it doesn't go as far as Rasmussen would have. Here, the selection of corporate form would govern only fiduciary duties in bankruptcy. *See* Robert K. Rasmussen, *Debtor's Choice: A Menu Approach to Corporate Bankruptcy*, 71 TEX. L. REV. 51, 66–67 (1992). For a discussion of the additional wave of debate provoked by contractualism, see Hampson & Katz, *supra* note 121, at 37 n.192.

[241] *See* LoPucki, *supra* note 127, at 757–58. LoPucki drew from the institutional economics literature, *see, e.g.*, Armen A. Alchian & Harold Demsetz, *Production, Information Costs, and Economic Organization*, 62 AM. ECON. REV. 777, 779–81 (1987), and from its application for corporate governance by Professors Margaret Blair and Lynn Stout, *see* Margaret M. Blair & Lynn A. Stout, *A Team Production Theory of Corporate Law*, 85 VA. L. REV. 247 (1999); Margaret M. Blair & Lynn A. Stout, *Team Production in Business Organizations: An Introduction*, 24 J. CORP. L. 743 (1999).

B. Caps for Sale

I have previously described the path through bankruptcy for a benefit corporation as a "hybrid" model, wherein a benefit corporation must continue to balance moneymaking against the specific or general public benefit set forth in its charter, while (of course) following the myriad rules the apply in a bankruptcy case.[242] To that model I am now adding the notion of stacked fiduciary duties, where trustees, DIPs, and committee members all wear multiple caps, something like the peddler in the famous 1940 children's book *Caps for Sale* — except fortunately for all involved, only two caps instead of a dozen.[243] This approach is admittedly complex, but I think it is the best way to make sense of fiduciary duties in bankruptcy: sorting through, methodically, the duties undertaken by the bankruptcy role and then layering those duties on top of any independent fiduciary duties.

On the other hand, one might argue, from a deontological perspective, that corporate purpose should give way to the discipline of repaying creditors as many dollars as possible. I do not think that conclusion follows so readily. Under either corporate or trust law, the duty is to act in the *best interests* of the obligee or beneficiary. And just as not all shareholders want to maximize stock value over all else, not all creditors want to maximize their bankruptcy distribution over all else.

One might argue, too, that this approach incentivize lenders to tighten terms on nonprofit corporations or benefit corporations *ex ante* — a result that might be worse for everyone on utilitarian grounds. For example, financial creditors might insist on taking a security interest in collateral more frequently for nonprofits or benefit corporations. The extent to which that might happen (and the degree to which it would be a problem) is an empirical

[242] Hampson, *supra* note 7, at 127. Lastly, bankruptcy proceedings are governed by dozens and dozens of rules, rules which constrain the discretion of the key players. Fiduciary duties do not solve all problems, and no one would seriously try to put that burden on them. As noted above, several scholars think the heavier sticks of motions to appoint a trustee or motions to convert are more likely to hold bankruptcy fiduciaries to their obligations. *See supra* Section __. Even if that's right, clarifying the nature and scope of fiduciary duties can only make those mechanisms more effective. As to appointment, breach of fiduciary duties could form a basis for a motion either for cause, *see* 11 U.S.C. § 1104(a)(1), or in the interests of the estate, *id.* § 1140(a)(2). As to conversion or dismissal, breach of fiduciary duties could form a basis for a motion for cause. *See* 11 U.S.C. § 1112(b)(1) & (4)(B) (defining cause to include "gross mismanagement of the estate").

[243] I do not mean to overstate the novelty of this metaphor. The image of bankruptcy fiduciaries wearing multiple "hats" is a common one, something I heard frequently in practice and that is reflected in the literature. *See, e.g.*, Lubben, *supra* note 46, at 25 ("The debtor as entity remains a creation of state law, but undertakes new obligations that are functions of federal law — a situation that results in the debtor and its management wearing more than its fair share of hats.").

question. Even if it does result in a higher cost of capital or some degree of credit rationing, we might celebrate that result as an efficient way to price in any costs of social enterprise on the front end.

For me, the most fruitful way of thinking about these questions comes not from deontological or utilitarian ethics, but from aretaic (or virtue) ethics, which focuses on ethical actors not as decisionmakers but as habitformers.[244] One of the functions of both organizational law and fiduciary law is to allow people with common values and shared visions to come together to build something of communal value — the channelling function of law as applied to the corporate law context.[245] And while the corporate form is frequently used for moneymaking, the development in commercial law to carve out space for where pecuniary interests may come alongside other values seems a salubrious advance in the law. Correspondingly, for it to evaporate upon a bankruptcy filing seems a waste.

CONCLUSION: A NEW OLD VISION FOR BUSINESS BANKRUPTCY

Since its inception, American business bankruptcy has been about preserving value. The upshot of this article, that varying perspectives on value should be honored in bankruptcy court, may seem new, but is actually consistent with the long trajectory of American corporation law and American bankruptcy law.

Consider the 1993 case of *After Six*, over thirty years ago. After Six was a manufacturer of formal wear which ceased operations because of large economic losses stemming from its competitor, AS Licensing Corp.[246] In a

[244] *See, e.g.*, Hampson, supra note 7, at 126–127 & n.172 (describing the relationship between the channelling function of law and virtue ethics); Michael G. Cartwright, *Afterword: Stanley Hauerwas's Essays in Theological Ethics: A Reader's Guide*, *in* STANLEY HAUERWAS, THE HAUERWAS READER 623, 625 (John Berkman & Michael Cartwright eds., 2001) (describing theological ethics as "*learning a new language* for describing the moral world").

[245] Professor Carl Schneider theorized the "channelling function of law" in a seminal article on family law in 1992. *See* Carl E. Schneider, *The Channelling Function in Family Law*, 20 HOFSTRA L. REV. 495, 497–98 (1992). The notion was given a new label by Schneider but is reminiscent of the *numerus clausus* principle, *see* Thomas W. Merrill & Henry E. Smith, *Optimal Standardization in the Law of Property: The Numerus Clauses Principle*, 110 YALE L.J. 1, 3 (2000), as well as Israeli legal philosopher Joseph Raz's second function of law, "providing facilities for private arrangements between individuals," JOSEPH RAZ, THE AUTHORITY OF LAW: ESSAYS ON LAW AND MORALITY 169–72 (1979); *see also* Blair & Stout, *supra* note 87, at 1787 (noting that "trust-based analysis suggests that the central purpose of fiduciary law is to induce trust behavior by social framing fiduciary relationships as relationships in which the law expects the fiduciary to internalize a commitment to pursue her beneficiary's interests rather than her own").

[246] *In re* After Six, 154 B.R. 876 (Bankr. E.D. Pa. 1993).

sale pursuant to section 363(b) of the Bankruptcy Code, AS Licensing Corp submitted the highest bid to buy the debtor and the DIP accepted. The lower bid was submitted by Genesco Inc., which included an offer of continuing employment to the debtor's current employees and was heavily supported by the Official Committee of Unsecured Creditors.[247] The court "with a heavy heart" said it was "compelled to conclude" that it must authorize the sale to AS Licensing Corp, recognizing that such a sale would likely close the debtor's local plant, destroying many textile workers' jobs.[248]

The *After Six* court reasoned that deference to a DIP's decision must be honored unless it is proven that the DIP abused that discretion. Accepting the highest bid could not generally form the basis for abuse of discretion. At the same time, it is clear that the *After Six* court struggled with the implications of affirming the DIP's choice of bidder. The court called the committee's position "socially responsible" and that the consensus of 80% of the committee's creditor members would have been sufficient to support a plan with a sale to Genesco.[249]

Ultimately, the court could not say that the DIP abused its discretion by selling to the highest bidder. Yet the court believed that it could award an auction to the lower bidder when that bid had other supporting factors, such as "society needs" in its favor. As the court said, "The Bankruptcy Code, like any law, must be read in its context as a tool of mankind, not a body of edits to which mankind is a slave."[250]

Both the *Bakalis* court and the *After Six* court recalled a broad conception of value — not only dollar amounts of the bids but likelihood of continued operations, job preservation, and even the ethics of keeping smaller businesses in the hands of those who care most about them.

When nonprofit or benefit debtors, creditors, or trustees start to push on their vision of value, much of standard bankruptcy practice will have to be rethought. This Article has tried to lay out the structure and context for some of that rethinking. In the end, as with so much of law, the question may turn not only on hard rules, but also on shared values.

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[247] *Id.* at 880. The Committee argued that it was "a more appropriate representative of the creditor body than the cadaverous Debtor, and that therefore its exercise of discretion should be preferred." *Id.* at 881.

[248] *Id.* at 878.

[249] *Id.* at 882.

[250] *Id.*