Committee Capture? An Empirical Analysis of the Role of Creditors' Committees in Business Reorganizations

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INTRODUCTION

Using a committee consisting of a business debtor's largest creditors to facilitate a financial restructuring agreement between the debtor and its creditors is not a new concept. In the early 1900s, equity receiverships performed a similar function, and creditors' committees were subsequently incorporated into the U.S. Bankruptcy Code.[1] Although the committee structure holds the promise of representation and cooperation, creditors' committees are, and to some extent always have been, vulnerable to manipulation, conflict, and self-interest.[2] Anecdotal evidence suggests that these abuses are on the rise. Consider the following:

FiberMark, Inc., a producer of specialty fiber-based materials, filed a Chapter 11 bankruptcy case on March 30, 2004, with approximately $185 million in assets and $359 million in liabilities.[3] The vast majority of FiberMark's liabilities were concentrated in two public bond issuances aggregating approximately $346 million.[4] Those bonds in turn were heavily traded in the secondary market both immediately before and during FiberMark's Chapter 11 case.[5]

The U.S. trustee initially appointed two of FiberMark's bondholders—AIG Global Investment Corp. and Post Advisory Group LLC—and the indenture trustee of those bond issuances to FiberMark's five-member creditors' committee.[6] AIG and Post collectively owned thirty-four percent of FiberMark's bond debt, with Post acquiring its fifteen percent holdings during the first quarter of 2004.[7] The original committee also included two of FiberMark's trade creditors—E.I. DuPont de Nemours & Company and Solution Dispersions, Inc.[8]

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1. *See infra* Part II.A.

2. For an overview of the committee structure under Chapter 11 of the Bankruptcy Code, see Kenneth N. Klee & K. John Shaffer, *Creditors' Committees Under Chapter 11 of the Bankruptcy Code*, 44 S.C. L. REV. 995 (1993).

3. Schedules of Assets & Liabilities & Schedule of Executory Contracts & Unexpired Leases, *In re* FiberMark, Inc., No. 04–10463 (Bankr. D. Vt. May 14, 2004).

4. *Id.* sched. F.

5. Report of Harvey R. Miller, as Examiner at 4–5, 8, *FiberMark*, No. 04–10463 (Aug. 16, 2005) [hereinafter Miller Report] (describing activity in secondary bond market). Buying and trading in the debt of financially distressed companies like FiberMark is a common investment strategy. *See generally* Michelle M. Harner, *The Corporate Governance and Public Policy Implications of Activist Distressed Debt Investing*, 77 FORDHAM L. REV. 703 (2008) (describing the activities of distressed debt investors).

6. Appointment of Committee of Unsecured Creditors, *FiberMark*, No. 04–10463 (Apr. 7, 2004) [hereinafter Committee Appointment].

7. Miller Report, *supra* note 5, at 4.

8. Committee Appointment, *supra* note 6.

Shortly after the appointment of the committee, FiberMark and DuPont reached an agreement that allowed DuPont to set off and thereby satisfy a large portion of its claim against FiberMark.[9] The court approved that agreement on June 14, 2004,[10] and DuPont resigned from the committee on June 24, 2004.[11] The U.S. trustee ultimately appointed Silver Point Capital, LP to fill DuPont's seat on the committee.[12] Silver Point acquired over thirty-five percent of FiberMark's bond debt on the secondary market.[13]

FiberMark proposed a plan of reorganization that contemplated an exchange of its unsecured debt for a combination of new debt and the equity of the reorganized company.[14] Consequently, AIG, Post, and Silver Point, as FiberMark's largest unsecured creditors, stood to become the largest shareholders of reorganized FiberMark. AIG and Post then engaged in a control contest against Silver Point.[15] This disagreement regarding who would control the reorganized company completely stalled FiberMark's reorganization efforts and cost its creditors an estimated $60 million.[16]

Given the contentious impasse, the court appointed an examiner to investigate, among other things, "the dispute among Committee members regarding corporate governance issues and whether any Committee member breached its fiduciary duty to act in the best interest of all creditors."[17] The examiner concluded that AIG

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9. Joint Motion of Debtors & E.I. DuPont De Nemours & Co. for Entry of Order Permitting Setoff of Mutual Obligations, *FiberMark*, No. 04–10463 (May 21, 2004).

10. Order Permitting E.I. DuPont De Nemours & Co. to Setoff Obligations Owing to & From Debtors, *FiberMark*, No. 04–10463 (June 14, 2004).

11. Second Amended Appointment of Committee of Unsecured Creditors, *FiberMark*, No. 04–10463 (June 24, 2004); *see also* Miller Report, *supra* note 5, at 28 ("On June 24, 2004, DuPont, after its claim was satisfied, resigned as a member of the Committee.").

12. Third Amended Appointment of Committee of Unsecured Creditors, *FiberMark*, No. 04–10463 (Oct. 27, 2004).

13. *See* Miller Report, *supra* note 5, at 8 ("The increase in Silver Point's position was viewed by Mr. Musante as 'a tad convenient.' ").

14. *See* First Proposed Disclosure Statement with Respect to Joint Plan of Reorganization Under Chapter 11, Title 11, United States Code of Fibermark, Inc., et al., Debtors, *FiberMark*, No. 04–10463 (Nov. 12, 2004).

15. *See FiberMark*, No. 04–10463, 2005 Bankr. LEXIS 652, at *4–6 (Bankr. D. Vt. Apr. 13, 2005) (describing dispute among creditors' committee members regarding alleged breaches of fiduciary duties and claims trading order); Miller Report, *supra* note 5, at 2–12.

16. Miller Report, *supra* note 5, at 12.

17. Order Directing the Appointment of an Examiner & Specifying Examiner's Duties Pursuant to § 1004(c) & § 1106(b) of the Bankruptcy Code, *FiberMark*, No. 04–10463 (Apr. 19, 2005). Section 1104(c) of the Bankruptcy Code provides:

> If the court does not order the appointment of a trustee under this section, then at any time before the confirmation of a plan, on request of a party in interest or the United States trustee, and after notice and a hearing, the court shall order the appointment of an examiner to conduct such an investigation of the debtor as is appropriate . . . .

and Post both breached their fiduciary duties.[18] Specifically, the examiner found that "AIG breached its fiduciary duties by using the Committee as a tool to accomplish its own agenda and seek benefits for itself, particularly in connection with the corporate governance issues and the pursuit of trading allegations against Silver Point."[19] He reached a similar conclusion with respect to Post.[20]

In addition to faulting AIG and Post, the examiner also reprimanded counsel to the committee, Akin, Gump, Strauss, Hauer, & Feld, LLP.[21] The examiner opined that

> Akin failed to discharge its obligations and perform its services in an independent, objective and disinterested manner as attorneys for the Committee by aligning itself with AIG and Post, particularly in respect of the corporate governance controversy and the assertion of Trading Order violations and breaches of fiduciary duties by Silver Point.[22]

The ultimate settlement gave Silver Point control of the reorganized company,[23] and, in a separate settlement, Akin agreed to forego $1.7 million in fees and expenses.[24]

The *FiberMark* case illustrates several potential abuses of the committee structure. Key creditors can use their committee membership to access information regarding the debtor's reorganization, obtain a seat at the plan negotiation table, and urge parties to pursue a reorganization that is beneficial to their own agendas. For instance, AIG allegedly sought to capture control of the committee and committee counsel for its own purposes. Moreover, even DuPont's service on the committee appears somewhat self-

11 U.S.C. § 1104(c) (2006).

18. *See* Miller Report, *supra* note 5, at 20–24 (setting forth the Examiner's conclusions).

19. *Id.* at 22.

20. *Id.* at 23 ("Post, in a similar fashion to AIG, acted in its own self interest in pursuing the imposition of corporate governance provisions on Silver Point and trading allegations against Silver Point, without consideration of the interests of all general unsecured creditors.").

21. *See id.* at 24 (describing Akin's failures).

22. *Id.*

23. Fourth Proposed Disclosure Statement with Respect to Amended Joint Plan of Reorganization Under Chapter 11, Title 11, United States Code of FiberMark, Inc., et al., Debtors at 52–54, *FiberMark*, No. 04–10463 (Sept. 23, 2005). AIG and Post agreed to contribute to a settlement fund and to sell their claims to Silver Point at a significant discount. *Id.*; *see also* Peter Lattman, *Bankrupt*, FORBES, Oct. 31, 2005, at 60, 60–62, *available at* http://www.forbes.com/forbes/2005/1031/060.html (describing Chapter 11 examiner's criticism of committee counsel's role in creditors' disputes in the *FiberMark* case).

24. Order Granting Motion to Approve Compromise & Settlement, Granting in Part, Denying in Part Application for Compensation for Akin Gump Strauss Hauer & Feld LLP, *FiberMark*, No. 04–10463 (Mar. 10, 2006). Akin originally requested $4,603,988.75 in fees and $443,754.24 in expenses for its services during the Chapter 11 case. Final Application for Compensation for Akin Gump Strauss Hauer & Feld LLP at 2, *FiberMark*, No. 04–10463 (Sept. 9, 2005).

motivated, as it resigned from the committee immediately upon accomplishing its own objective. This type of turnover of committee membership can cause instability and potentially expose the committee to further manipulation by other creditors.[25]

Anecdotal evidence suggests that *FiberMark* is not an isolated case.[26] Nevertheless, no prior empirical studies evaluate the conduct, activities, or abuses of creditors' committees in Chapter 11 cases.[27] The study in this Article fills that void and provides valuable insight into the role of creditors' committees in Chapter 11 cases.

Part I of this Article sets forth the primary findings of the study. Part II then provides the background for the study by explaining the historical development of creditors' committees and their contemplated role in the business reorganization process. This part also summarizes the prior studies concerning Chapter 11 cases that touch aspects of the committee structure. Part III describes the methodology underlying the study, and Part IV presents the data. The study suggests that, in certain cases, creditors' committees can add value to the reorganization process, but it also highlights several weaknesses in the committee structure that can impair or reallocate value. Part V explores these issues and offers suggestions for policy changes and further study.

I. SUMMARY OF KEY FINDINGS

A creditors' committee is designed to protect and promote the interests of general unsecured creditors.[28] Since 1978, the U.S. trustee has appointed creditors' committees in some but not all Chapter 11 cases, and the participants largely have assumed the prudence and

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25. *See infra* Part V.

26. Many cases are discussed *infra* Part II.B. *See also* Westmoreland Human Opportunities, Inc. v. Walsh, 327 B.R. 561, 568–76 (W.D. Pa. 2005) (allegations of breach of duty based on committee member's conflicts of interest); *In re* Venturelink Holdings, Inc., 299 B.R. 420, 422 (Bankr. N.D. Tex. 2003) (former insider of debtor wanted and initially received appointment to creditors' committee); *In re* Fas Mart Convenience Stores, Inc., 265 B.R. 427, 429–30 (Bankr. E.D. Va. 2001) (committee opposed appointment of additional member who held large claim against debtor and interests that conflicted with other unsecured creditors); *In re* Papercraft Corp., 129 B.R. 56, 56–58 (Bankr. W.D. Pa. 1991) (committee brought litigation against one of its members who secretly purchased claims worth millions of dollars against the debtor at a significant discount to the detriment of the debtor and its stakeholders); Complaint at 9–11, 13–14, *In re* Galey & Lord, No. 02–40445 (AJG) (S.D.N.Y. Nov. 6, 2003) (alleged breach of duty by committee member for using confidential information to advance its own interests).

27. *See infra* Part II.C.

28. *See infra* Part II.A.

effectiveness of those appointments. The data suggest, however, that the role of creditors' committees warrants a closer look.[29]

The study includes 296 Chapter 11 cases, with 152 of those cases involving one or more committees.[30] Several analyses categorize cases by committee type (no committee, single creditors' committee, and multiple or other committee cases) for comparative purposes and control for factors other than committee activity that might influence outcomes. Other analyses focus on emerging trends in the data for all cases. Part IV sets forth detailed analyses of the key data, and Part V discusses their potential policy implications.

With respect to case duration, cases with no committees had significantly shorter overall durations, but required significantly longer periods of time to resolve motions to sell substantially all of the debtor's assets.[31] The lack of a committee did not impact the time between the filing of a Chapter 11 case and confirmation of any plan of reorganization or liquidation.[32] Nevertheless, cases with no committees were significantly less likely to have at least one formal request for an extension of the debtor's exclusive periods to file and solicit votes on a plan.[33]

Cases with a single creditors' committee were significantly more likely than the other two categories to result in a plan of liquidation or a motion to sell substantially all of the debtor's assets.[34] This result remained even after controlling for asset size and approval of debtor-in-possession ("DIP") financing.[35] Those cases also were significantly more likely to provide distributions to unsecured creditors in amounts less than or equal to fifty percent of their claim values.[36]

The data also show discernible instances of potential conflicts of interest held by committee members, and track litigation filed by creditors' committees against secured creditors and debtors.[37] Although both conflicts and litigation significantly increased the estate's professional fees and expenses, they did not significantly

29. *See infra* Part IV.

30. *See infra* Part IV.B.

31. *See infra* Part IV.C. Analyses are based on comparative categories.

32. *See infra* Part IV.C.1. Analyses are based on comparative categories.

33. *See infra* Part IV.C.1. Analyses are based on comparative categories.

34. *See infra* Part IV.C.3.

35. For an explanation of the multivariate analyses, see *infra* Part IV.C.3. The data analysis also considered other possible confounding variables such as the number of creditors, liabilities and secured claims. *See infra* Part IV.C.3.

36. *See infra* Part IV.C.4. This result remained after controlling for identified confounding variables. *See infra* Part IV.C.4.

37. *See infra* Part IV.D.

affect whether a debtor reorganized or liquidated or the percentage recovery to general unsecured creditors.[38] The data on creditors' committee litigation against debtors do suggest, however, that committees are fulfilling at least part of their oversight responsibilities with some zeal.

The lack of a strong association between conflicts and disputes, on the one hand, and value, on the other, in Chapter 11 cases supports digging deeper into the data and anecdotal evidence to explain the effect of creditors' committees on Chapter 11 cases.[39] Part V engages in this analysis and considers, among other things, the potential influence of the identity of committee members, the dynamics of committee versus no-committee cases, and disclosure obligations. It concludes by encouraging more strategic decisions regarding the role of multiple committees and the composition of single committees in Chapter 11 cases and highlighting the value of increased disclosure obligations for all Chapter 11 participants.

II. A HISTORICAL OVERVIEW OF CREDITORS' COMMITTEES

The concept of a creditors' committee has great appeal. It signifies representation and cooperation—key elements of most successful debt restructuring plans. It also presents a potential solution to the collective action problem that often impairs debt restructuring efforts.[40] Nevertheless, in many cases, the committee structure appears to fail its intended beneficiaries.[41]

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38. *See infra* Part IV.D.3. Notably, cases involving committee litigation against the debtor also are significantly longer than cases without such litigation. *See infra* Part IV.D.3.

39. *See infra* Parts IV.D, V.

40. Collective action problems arise for creditors of troubled companies because those creditors often are dispersed and the cost of collection efforts may outweigh the value of any individual creditor's claim against the company. *See generally* David Arthur Skeel, *The Nature and Effect of Corporate Voting in Chapter 11 Reorganization Cases*, 78 VA. L. REV. 461 (1992) (explaining collective action problems in both the shareholder and creditor context, as well as the contemplated role of creditors' committees in this context). These and other factors can discourage individual creditor involvement and impede individual creditor effectiveness in the debt restructuring process. The Bankruptcy Code seeks to use the committee structure to address at least part of this collective action problem. *See* Elizabeth Warren, *Bankruptcy Policymaking in an Imperfect World*, 92 MICH. L. REV. 336, 347 (1993) ("The creditors' committee is designed to accomplish effective creditor involvement at the lowest possible costs."); *see also* Lynn M. LoPucki & William C. Whitford, *Corporate Governance in the Bankruptcy Reorganization of Large, Publicly Held Companies*, 141 U. PA. L. REV. 669, 680 (1993) (discussing the collective action problem and the role of creditors' committees in drafting reorganization plans); Stephen J. Lubben, *Credit Derivatives and the Future of Chapter 11*, 81 AM. BANKR. L.J. 405, 421 (2007) (discussing collective action problem); Robert K. Rasmussen & Randall S. Thomas, *Timing Matters: Promoting Forum Shopping by Insolvent Corporations*, 94 NW. L. REV. 1357, 1394 (2000) ("The Bankruptcy Code's solution to this collective action problem is to place

This Part summarizes the development of the creditors' committee and its governance role in the Chapter 11 process. This discussion leads to a brief overview of the perceived flaws in the committee structure and the prior empirical studies that reference Chapter 11 committee performance.[42] The background information provided here underscores the importance of the study reported in this Article and facilitates a more meaningful analysis of the data.

A. The Historical Development of Creditors' Committees

The relationship between a corporation and its creditors largely is governed by negotiated contract terms.[43] As long as the corporation is solvent and complying with the terms of its various creditor contracts, the corporation's board of directors and management can focus on operating the business and maintaining the corporation's relationship with its shareholders.[44] Once the corporation experiences financial distress, however, this focus frequently shifts to managing the corporation's relationship with its creditors—a daunting task for most corporations.[45] The following discussion summarizes the role of

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the drafting of a large, publicly held company's reorganization plan in the hands of creditors' committees.").

41. *See, e.g.*, Christopher W. Frost, *The Theory, Reality and Pragmatism of Corporate Governance in Bankruptcy Reorganizations*, 72 AM. BANKR. L.J. 103, 119–24 (1998) (discussing persistence of collection action problems in Chapter 11, including shareholder apathy and conflict between corporate governance norms and the primary goals of the Bankruptcy Code).

42. *See infra* Parts II.B, C.

43. *See, e.g.*, Katz v. Oak Indus., Inc., 508 A.2d 873, 876–79 (Del. Ch. 1986) ("Under our law—and the law generally—the relationship between a corporation and the holders of its debt securities, even convertible debt securities, is contractual in nature.").

44. *See, e.g.*, Frost, *supra* note 41, at 107–10 (1998) (explaining the inherent conflict between creditors and shareholders and discussing management's role in mitigating this conflict through "[management's] control over the selection of business projects [that] enables them to choose between satisfying the shareholders' appetite for risk and observing the creditors' distaste for such projects").

45. *See id.* (discussing governance challenges in insolvency context); *see also* Kelli A. Alces, *Strategic Governance*, 50 ARIZ. L. REV. 1053, 1054–60 (2008) (same); Steven L. Schwarcz, *Rethinking a Corporation's Obligations to Creditors*, 17 CARDOZO L. REV. 647, 651–60 (1996) (reflecting on the boundaries of corporate obligations to creditors, especially where they conflict with obligations to shareholders). Courts and commentators debate whether management's fiduciary duties, as well as their focus, shift to creditors at any point as a company's finances deteriorate. *See, e.g.*, N. Am. Catholic Educ. Programming Found., Inc. v. Gheewalla, 930 A.2d 92, 103 (Del. 2007) (stating that a solvent or nearly solvent corporation owes no duties to creditors); Rutherford B. Campbell, Jr. & Christopher W. Frost, *Managers' Fiduciary Duties in Financially Distressed Corporations: Chaos in Delaware (and Elsewhere)*, 32 J. CORP. L. 491, 508–12 (2007) (discussing courts' different treatment of boards' fiduciary duties to shareholders and creditors); Henry T.C. Hu & Jay Lawrence Westbrook, *Abolition of the Corporate Duty to Creditors*, 107 COLUM. L. REV. 1321, 1332–35 (2007) (same); Jonathan C. Lipson, *Directors' Duties to Creditors: Power Imbalance and the Financially Distressed Corporation*, 50 UCLA L.

creditors' committees prior to the enactment of federal corporate reorganization laws, under the Bankruptcy Act of 1898, and then under the current Bankruptcy Code.

1. Committees and Equity Receiverships

A corporation's creditors typically are widely dispersed with various (often competing) economic interests and agendas. Consequently, even before Congress incorporated business reorganization provisions into federal bankruptcy laws, business managers themselves embraced the concept of a creditors' committee.[46] Early committees frequently were self-selected, limited to a particular tranche of debt, and not necessarily formed to represent the interests of the corporation's general creditor body.[47]

For example, in the early 1900s, corporations used a process commonly called "equity receivership" to restructure their debt obligations. Under this process, a creditor filed a receivership petition against the corporation in the federal district court, which then appointed a receiver for the eventual sale of the company to the highest bidder.[48] In practice, this process often was orchestrated between the corporation's management and creditors that were friendly to management.[49] Those creditors would petition the court for the receivership and form a protective or reorganization committee. In most cases, the reorganization committee, working with management, would be the successful bidder at the receivership sale.[50] The end

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REV. 1189, 1236 (2003) (proposing that duties be based not on priorities but on "imbalances of volition, cognition, and exit"); Frederick Tung, *The New Death of Contract: Creeping Corporate Fiduciary Duties for Creditors*, 57 EMORY L.J. 809, 825 (2008) (explaining boards' fiduciary duties to shareholders versus creditors and arguing against any expansion of such duties to creditors).

46. *See, e.g.*, DAVID A. SKEEL, JR., DEBT'S DOMINION 56–60 (2001) (explaining equity receivership process); Donald R. Korobkin, *Rehabilitating Values: A Jurisprudence of Bankruptcy*, 91 COLUM. L. REV. 717, 747–49 (1990) (same); Bruce A. Markell, *Owners, Auctions and Absolute Priority in Bankruptcy Reorganizations*, 44 STAN. L. REV. 69, 74–77 (1991) (same); Charles Jordan Tabb, *The History of the Bankruptcy Laws in the United States*, 3 AM. BANKR. INST. L. REV. 5, 21–23 (1995) (same).

47. *See* Daniel J. Bussel, *Coalition-Building Through Bankruptcy Creditors' Committees*, 43 UCLA L. REV. 1547, 1553–55 (1996) (explaining committee role in equity receiverships).

48. *See supra* notes 46–47; *see also* Michelle M. Harner, *The Search for an Unbiased Fiduciary in Corporate Reorganizations*, 86 NOTRE DAME L. REV. (forthcoming 2011), *available at* http://ssrn.com/abstract=1492701 (explaining historical development of creditors' committee in bankruptcy).

49. *See* Tabb, *supra* note 46, at 22 ("In practice, the equity receivership came to be dominated by insiders, and was subject to much abuse.").

50. *Id.* ("In form, the receivership resulted in the sale of the debtor's assets, with the proceeds distributed to creditors. In substance, however, the entire elaborate proceeding often

result allowed management and the reorganization committee to maintain control of the corporation while cashing out dissenting creditors at a discounted price.

The use of committees in the equity receivership process garnered significant criticism. The most vocal critic arguably was Justice Douglas while he was working at the Securities and Exchange Commission ("SEC").[51] Justice Douglas believed that management and large creditors abused the receivership process by closing out dissenting creditors and chilling competitive bidding.[52] In most cases, dissenting creditors were forced out through a cash payment representing a significant discount on the face value of their claim against the company.[53] Rather than maximizing entity value for existing stakeholders, equity receiverships at their worst reallocated that value to insiders and key creditors.

2. Committees and the Bankruptcy Act of 1898

Although Congress initially incorporated a business reorganization chapter into federal bankruptcy law that was based on the equity receivership process, it ultimately discarded that approach in favor of a more paternal approach, at least for large public companies.[54] The change in approach arose in part from Justice Douglas's concern about conflicts of interest.[55] As a result, Chapter X of the Bankruptcy Act of 1898, which applied to large public

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resulted in old management retaining control of the enterprise, and dictating the terms of the sale.").

51. *See* Bussel, *supra* note 47, at 1556–57 (discussing abuses of process identified by Justice Douglas during his tenure with the SEC).

52. Justice Douglas observed, "In the welter of conflicting interests, ulterior objectives, and self-serving actions which flow from investment banker-management dominance over committees, these committees have lost sight of their essential functions which they can perform to advance the interests of investors." *To Amend the Securities Act of 1933: Hearing on H.R. 6968 Before the H. Interstate and Foreign Commerce Comm.*, 75th Cong. 24 (1937) (statement of William O. Douglas).

53. *See* SKEEL, *supra* note 46, at 60 (explaining the practice of paying "upset price" to dissenting creditors).

54. *See* Bussel, *supra* note 47, at 1555–56 ("[Section 77B was] aptly described as 'the old equity receivership reorganization process pressed upon a bankruptcy mold, with additions.' ") (quoting Carl D. Friebolin, *Section 77B: Sword or Shield*, 10 J. NAT'L ASS'N REF. BANKR. 79, 79 (1936)).

55. *See* SKEEL, *supra* note 46, at 106–09 (discussing the process to revamp section 77B); Tabb, *supra* note 46, at 28–30 (describing efforts to rework section 77B, including Douglas's investigation of the committee); *see also* SEC, REPORT ON THE STUDY AND INVESTIGATION OF THE WORK, ACTIVITIES, PERSONNEL AND FUNCTIONS OF PROTECTIVE AND REORGANIZATION COMMITTEES § IV (1937) (summarizing the strategy and techniques of reorganization).

companies, did not include a formal role for creditors' committees.[56] Instead, creditors' committees played a nominal role in Chapter X cases.

Notably, Congress maintained the formal role of creditors' committees in the context of small business reorganizations codified in Chapter XI of the Bankruptcy Act. Unlike Chapter X, which was largely controlled by an independent trustee and the SEC, Chapter XI reorganizations were directed primarily by the business debtor and its creditors' committee.[57] Chapter XI charges creditors' committees with overseeing the conduct of the debtor and negotiating the debtor's plan of reorganization; for the most part, they were active participants in cases.[58] Commentators attribute the level of committee activity in Chapter XI cases to the absence of a trustee or other formal monitoring of the debtor.[59]

3. Committees and the Bankruptcy Code

The Chapter XI approach to business reorganization, including its formal role for creditors' committees, prevailed when Congress overhauled federal bankruptcy laws in 1978.[60] The business reorganization sections were collapsed into one chapter—the current Chapter 11 of the Bankruptcy Code—that contemplates the appointment of a creditors' committee in every business reorganization case.[61] Specifically, section 1102 of the Bankruptcy Code states that "the United States trustee shall appoint a committee of creditors holding unsecured claims . . . . ordinarily consist[ing] of the persons, willing to serve, that hold the seven largest claims

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56. SEC v. Am. Trailer Rentals Co., 379 U.S. 594, 603–06 (1965) (explaining the development of the Chandler Act); Bussel, *supra* note 47, at 1557–58 (explaining key elements of Chapter X).

57. *See* Bussel, *supra* note 47, at 1557–58 (explaining key elements of Chapter XI); *see also* A. Mechele Dickerson, *Privatizing Ethics in Corporate Reorganizations*, 93 MINN. L. REV. 875, 888–89 (2009) (describing treatment of debtors and their management under Chapter X versus Chapter XI).

58. Creditors' committees under Chapter XI were either elected by general unsecured creditors or, if no elections were held, appointed by the court. *See* RICHARD F. BROUDE, REORGANIZATION UNDER CHAPTER 11 OF THE BANKRUPTCY CODE § 3.02[1] (2005) (explaining the selection and changes in composition of committees).

59. *See id.* ("Experience under the . . . Bankruptcy Act had been that creditors' committees were more active in Chapter XI cases than Chapter X reorganization cases because, in the latter, the trustee played the primary role in proposing and confirming a plan of reorganization.").

60. *See* SKEEL, *supra* note 46, at 136–45 (describing process and substantive decisions relating to enactment of the Bankruptcy Code); Tabb, *supra* note 46, at 35–36 (discussing the changes made in the 1978 overhaul).

61. *See* Tabb, *supra* note 46, at 35 ("Another notable feature of the 1978 law was the merger of the reorganization chapters into a single chapter.").

against the debtor of the kinds represented on such committee."[62] The U.S. trustee also may appoint additional statutory committees of creditors or shareholders.[63]

Chapter 11 of the Bankruptcy Code permits a troubled company and its management to stay in possession and control of the company's assets and operations during the reorganization process.[64] Thus, the company operates as a "debtor in possession."[65] The bankruptcy court may appoint a trustee or examiner to investigate or run a debtor's business, but those appointments are the exception to the general debtor-in-possession rule.[66]

Nevertheless, Chapter 11 does not contemplate unfettered control for the debtor in possession. Most major transactions require approval of the bankruptcy court, and the U.S. trustee oversees general case administration matters.[67] Moreover, Chapter 11 posits the creditors' committee as a "statutory watchdog," with authority to

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62. 11 U.S.C. § 1102(a)–(b) (2006).

63. *Id.* § 1102(a). For example, the U.S. trustee may appoint an official committee of trade creditors or an official committee of equity holders. The decision to appoint multiple committees frequently turns on the size of the Chapter 11 case, the level of creditor or shareholder interest and whether a single committee can sufficiently represent all of the different claims or interests. Although creditors' committees are the focus of this study, the data analyze different types of committees, including multiple creditors' committees, equity committees, and ad hoc committees. *See infra* Part IV.

64. *See, e.g.*, SKEEL, *supra* note 46, at 216–17 (discussing pro-debtor aspects of Chapter 11 in an historical context and noting that Chapter 11 of the Bankruptcy Code adopted "an explicitly manager-friendly approach to corporate reorganization"); J. Bradley Johnston, *The Bankruptcy Bargain*, 65 AM. BANKR. L.J. 213, 293 (1991) (explaining management control in Chapter 11 process and observing that "[m]anagement's postpetition control of a debtor's operations is complemented by specific, individual Code provisions which give management substantial control over the reorganization process itself"); LoPucki & Whitford, *supra* note 40, at 688–94 (explaining historical grounds for management control in Chapter 11 context); *see also* Harner, *supra* note 48 (manuscript at 27–32) (analyzing increased activism of debtholders and implications for corporate insolvencies in the United States and the United Kingdom); George W. Kuney, *Hijacking Chapter 11*, 21 BANKR. DEV. J. 19, 21–23 (2004) (explaining that "[s]ince [the Bankruptcy Code's enactment,] it has been portrayed as a debtor-friendly statute featuring a fresh start for debtors and the prospect of reorganization for businesses" and positing that such portrayal may be erroneous).

65. *See* § 1107(a)–(b) (explaining concept and duties of a debtor in possession).

66. § 1104(a) (appointment of Chapter 11 trustee); § 1104(c) (appointment of Chapter 11 examiner); § 1106(a)(1) (Chapter 11 trustee duties); *see also In re* Sharon Steel Corp., 871 F.2d 1217, 1225–29 (3d Cir. 1989) (affirming appointment of Chapter 11 trustee); Kelli A. Alces, *Enforcing Corporate Fiduciary Duties in Bankruptcy*, 56 KAN. L. REV. 83, 86 (2007) (noting that replacing a debtor-in-possession with a public trustee is "an extreme and expensive remedy"); Dickerson, *supra* note 57, at 898–900 ("Though the Code provides that managers can be replaced or supervised by a public trustee, trustee appointments are, and always have been, rare.").

67. *See, e.g.*, § 363(b) (requiring court approval of transactions outside of the ordinary course of business); § 1129 (requiring court approval of plan of reorganization).

investigate and monitor the DIP's conduct.[68] Among other things, the committee may: consult with the debtor; "investigate the acts, conduct, assets, liabilities, and financial condition of the debtor"; "participate in the formulation of a plan"; and "request the appointment of a trustee or examiner."[69]

The legislative history of Chapter 11 suggests that Congress intended the creditors' committee to give the general creditor body a stronger voice in the reorganization process.[70] Unsecured creditors rarely involved themselves in the reorganization, either because they were disinterested or not invited to the negotiation table.[71] Part of the purpose of section 1102 was to establish the committee as "a vital and integral part of the plan formulation process."[72]

The committee and its members are situated as fiduciaries for creditors they represent.[73] The U.S. trustee generally appoints

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68. Courts and commentators invoke the phrase "statutory watchdog" to describe the role of the creditors' committee. *See, e.g.*, *In re* AKF Foods, Inc., 36 B.R. 288, 289–90 (Bankr. E.D.N.Y. 1984) ("The function of a creditors' committee is to act as a watchdog on behalf of the larger body of creditors which it represents."); W. Michael Schuster, *For the Greater Good: The Use of Public Policy Considerations in Confirming Chapter 11 Plans of Reorganization*, 46 HOUS. L. REV. 467, 495 (2009) (quoting the phrase as used in various cases).

69. § 1103(c) (setting forth powers of committee); *see also* BROUDE, *supra* note 58, §3.02[4] (explaining powers granted creditors' committees under § 1103).

70. The legislative history to § 1102 provides:

> This section provides for the appointment of creditors' and equity security holders' committees, which will be the primary negotiating bodies for the formulation of the plan of reorganization. They will represent the various classes of creditors and equity security holders from which they are selected. They will also provide supervision of the debtor in possession and of the trustee, and will protect their constituents' interests.

H.R. REP. NO. 95–595, at 401 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6357.

71. " 'Creditors . . . take little interest in pursuing a bankruptcy debtor. They are unwilling to throw good money after bad.' " Lynn M. LoPucki, *The Debtor in Full Control—Systems Failure Under Chapter 11 of the Bankruptcy Code?*, 57 AM. BANKR. L.J. 247, 247 (1983) (quoting H.R. REP. NO. 95–595, at 92); *see also infra* note 101 and accompanying text (explaining factors contributing to committee ineffectiveness).

72. Retail Mktg. Co. v. Nw. Nat'l Bank (*In re* Mako, Inc.), 120 B.R. 203, 212 (Bankr. E.D. Okla. 1990); *see also* BROUDE, *supra* note 58, § 3.02[1] (explaining that the "drafters felt that creditors' committees should play a greater role in Chapter 11 cases"); Harvey R. Miller, *The Changing Face of Chapter 11: A Reemergence of the Bankruptcy Judge as Producer, Director, and Sometimes Star of the Reorganization Passion Play*, 69 AM. BANKR. L.J. 431, 449 (1995) ("The mandatory appointment of a creditors' committee was intended to provide dynamic tension with the debtor that would stimulate the reorganization process through effective and efficient oversight and negotiation.").

73. *See, e.g.*, *In re* Fas Mart Convenience Stores, Inc., 265 B.R. 427, 432 (Bankr. E.D. Va. 2001) ("Members of the committee also have another duty—a fiduciary duty to all creditors represented by the committee."); *In re* Firstplus Fin., Inc., 254 B.R. 888, 894 (Bankr. N.D. Tex. 2000) ("In a Chapter 11 case, an Unsecured Creditors' Committee is appointed by the Office of the United States Trustee and owes a fiduciary duty to act on behalf of all unsecured creditors."). For thoughtful discourse regarding issues posed by a fiduciary label for the committee and others in bankruptcy, see C.R. Bowles, Jr. & Nancy B. Rapoport, *Has the DIP's Attorney Become the*

members to the creditors' committee and determines the need for the appointment of any additional committees in the Chapter 11 case.[74] The U.S. trustee selects committee members based on the size and nature of the creditor's claims against the debtor and a questionnaire that the creditor itself completes.[75] A committee typically consists of seven to nine of the debtor's largest unsecured creditors.[76] These creditors may hold interests, however, that are adverse to the debtor or other members of the committee.[77]

The members of a creditors' committee can wield significant influence in a Chapter 11 case.[78] They obtain access to the debtor's

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Ultimate Creditors' Lawyer in Bankruptcy Reorganization Cases?, 5 AM. BANKR. INST. L. REV. 47, 53–54 (1997); *see also* Susan M. Freeman, *Are DIP and Committee Counsel Fiduciaries for Their Clients' Constituents or the Bankruptcy Estate? What is a Fiduciary, Anyway?*, 17 AM. BANKR. INST. L. REV. 291 (2009) (providing a detailed analysis of debtor in possession and committee as fiduciaries). In general, a fiduciary duty exists where "one party to a fiduciary relation (the *entrustor*) is dependent on the other (the fiduciary)." Tamar Frankel, *Fiduciary Law*, 71 CAL. L. REV. 795, 800 (1983).

74. § 1102(a)(1); *see also* Klee & Shaffer, *supra* note 2, at 1001–04 (providing a detailed analysis of the formation process); Greg M. Zipes & Lisa L. Lambert, *Creditors' Committee Formation Dynamics: Issues in the Real World*, 77 AM. BANKR. L.J. 229, 229–30, 239 (2003) (explaining committee formation process).

75. The U.S. trustee typically mails questionnaires to the debtor's largest creditors asking, among other things, about their interest in serving on the committee and the details of their claims against the debtor. U.S. TRUSTEE PROGRAM, U.S. DEP'T JUSTICE, UNITED STATES TRUSTEE MANUAL: CHAPTER 11 CASE ADMINISTRATION 3–4.2 to 3–4.4 (1998), *available at* http://www.justice.gov/ust/eo/ust_org/ustp_manual/docs/vol3.pdf.

76. *See* Klee & Shaffer, *supra* note 2, at 1005–06; Zipes & Lambert, *supra* note 74, 233–34.

77. *See, e.g.*, Robert P. Enayati, *Undermining the Trading Wall: The BAPCPA's Affront on the Creditors' Committee's Duty of Confidentiality in Chapter 11 Bankruptcies*, 21 GEO. J. LEGAL ETHICS 703, 706 (2008) (discussing issues posed by misappropriation of confidential information by, among others, creditors' committee members); Burke Gappmayer, *Protecting the Insolvent: How a Creditor's Committee Can Prevent Its Constituents from Misusing a Debtor's Nonpublic Information and Preserve Chapter 11 Reorganizations*, 2006 UTAH L. REV. 439, 445–46 (discussing conflicts of interest that may affect creditors' committee members); *see also* Carl A. Eklund & Lynn W. Roberts, *The Problem with Creditors' Committees in Chapter 11: How to Manage the Inherent Conflicts Without Loss of Function*, 5 AM. BANKR. INST. L. REV. 129, 130–33 (1997) (analyzing problems posed by committee member conflicts); Nancy B. Rapoport, *Turning and Turning in the Widening Gyre: The Problem of Potential Conflicts of Interest in Bankruptcy*, 26 CONN. L. REV. 913, 916–17 (1994) (examining conflict of interest issues in bankruptcy, including in committee context); Michael P. Richman & Jonathan E. Aberman, *Creditors' Committees Under the Microscope: Recent Developments Highlight Hazards of Self-Dealing*, AM. BANKR. INST. J., Sept. 2007, at 22 (examining Chapter 11 cases involving committee member conflicts of interest).

78. *See, e.g.*, John D. Ayer et al., *What Every Unsecured Creditor Should Know About Chapter 11*, AM. BANKR. INST. J., June 2004, at 16, 40 ("Because the fees for these professionals are paid by the chapter 11 debtor's estate, membership on the unsecured creditors' committee is probably the most cost-effective way for individual unsecured creditors to influence the outcome of a bankruptcy case and protect their interests."). Interestingly, the most popular response in the professional and committee member surveys regarding how creditors most frequently attempt to influence Chapter 11 cases was seeking appointment to the creditors' committee.

confidential and proprietary information; they are involved in negotiations regarding the debtor's reorganization; and their support generally is necessary for the debtor's successful reorganization.[79] Both the bankruptcy court and other general unsecured creditors rely on the committee and will, to varying degrees, defer to the committee's assessment.[80]

This influence can be used for the benefit of all unsecured creditors or, in some instances, the self-interest of the committee members.[81] In the latter scenario, a member can use its position to get the debtor's ear and, for example, convince the debtor to pay attention to that member's claims or contracts or even to pursue a particular restructuring course.[82] This influence can be subtle and hard to detect, but the consequences can be devastating for the debtor and its stakeholders.

B. The Many Roles of Committees

A creditors' committee can play a pivotal role in a Chapter 11 case. It can investigate the debtor's operations, review the debtor's business plan, and help the debtor evaluate viable restructuring options.[83] When that process reveals troubling information, the committee can seek the appointment of a Chapter 11 trustee, an

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79. *See, e.g.*, Brad B. Erens & Kelly M. Neff, *Confidentiality in Chapter 11*, 22 EMORY BANKR. DEV. J. 47, 72–77 (2005) (discussing the sharing of confidential information in Chapter 11 and related issues); John T. Hansen, *Pushing the Envelope of Creditors' Committee's Powers*, 80 AM. BANKR. L.J. 89, 91–92 (2006) (exploring the parameters of committee power in Chapter 11); Klee & Shaffer, *supra* note 2, at 1040–41 (discussing the powers and conduct of committees in Chapter 11 cases); Schuster, *supra* note 68, at 495–96 (explaining role of the committee in the plan process).

80. *See, e.g.*, Daniel J. Bussel & Kenneth N. Klee, *Recalibrating Consent in Bankruptcy*, 83 AM. BANKR. L.J. 663, 690 (2009) ("More recently, as chapter 11 practice has become more centered on financing orders and § 363 sales to which the statutory solicitation and voting procedures do not apply, the bankruptcy courts increasingly look to the creditors' committee as the proxy for unsecured creditor interests.").

81. Consider the following observations by one court:

> [T]he individuals constituting a committee should be honest, loyal, trustworthy and without conflicting interests, and with undivided loyalty and allegiance to their constituents. Conflicts of interest on the part of representative persons or committees are thus not . . . tolerated. Thus, where a committee representative or agent seeks to represent or advance the interest of an individual member of a competing class of creditors or various interests or groups whose purposes and desires are dissimilar, this fiduciary is in breach of his duty of loyal and disinterested service.

Johns-Manville Sales Corp. v. Doan (*In re* Johns-Manville Corp.), 26 B.R. 919, 925 (Bankr. S.D.N.Y. 1983) (citations omitted); *see also infra* note 85 and accompanying text (discussing pros and cons of serving on a creditors' committee).

82. *See* cases cited *infra* Part II.B.

83. *See supra* Part II.A.3.

examiner, or an alternative management team. The committee also can be an ally for the debtor in its negotiations with secured creditors and potential postpetition lenders or purchasers. Debtors often use the refrain, "Management would like to pursue this deal but the creditors' committee will never sign off on it."[84]

Just as frequently, however, a creditors' committee can be an antagonist to the debtor or other parties in interest.[85] This additional pressure may be warranted or it may be suspect and at the behest of specific committee members.[86] The *FiberMark* case described above illustrates committee conduct orchestrated by two members that arguably prolonged the debtor's case and decreased overall value.[87] Similar cases include the Chapter 11 cases of *American Manufacturers*, *Adelphia Communications*, *Galey & Lord*, and *WorldCom*.[88] In addition, conflict between the creditors' committee

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84. *See, e.g.*, WILLIAM T. THURMAN ET AL., CRITICAL ISSUES FACING THE CORPORATE CLIENT CONSIDERING CHAPTER 11 IN TODAY'S ECONOMY § II.A.2.e (Mar. 14, 2009), *available at* http://www.utahbar.org/cle/springconvention/materials/bankruptcy_section.pdf ("The Committee can be an extremely valuable ally or your worst enemy in the Debtor's efforts to reorganize. Communicating often and openly with the Committee's counsel will be a must for Debtor's counsel if the Debtor intends to succeed in its reorganization efforts.").

85. *See In re* SmartWorld Tech., LLC, 552 F.3d 228, 235 (2d Cir. 2009) (referring to bankruptcy court decision that explained the " 'divergent positions regarding litigation and settlement strategy . . . between the Debtor and the Committee' and the desire of the former to benefit its equity holders rather than its creditors" and noting that " 'some degree of antagonism and animosity between a debtor and creditor can be expected in any bankruptcy proceeding' . . . [because] both entities seek to maximize their shares of a finite (and always inadequate) pool of resources"); James M. Sullivan & Gary O. Ravert, *A Vendor's Guide to Bankruptcy*, 2006 BLOOMBERG CORP. L.J. 494, 499–500, *available at* http://www.mwe.com/info/pubs/bloomberg_sullivan_ravert.pdf (explaining pros and cons to serving on creditors' committee and noting, with the caveat of a member's fiduciary duty, that the committee's "increased access [to the debtor and its information] can often foster improved business relations between a committee member and the debtor both during a chapter 11 case and after a chapter 11 case is over").

86. For example, a creditors' committee may identify questionable prepetition conduct that supports the appointment of an examiner or trustee. *See, e.g.*, Dan Nakaso, *Hawaiian Air Creditors Seek Bankruptcy Trustee*, HONOLULU ADVERTISER, May 3, 2003, at A1, *available at* http://the.honoluluadvertiser.com/article/2003/May/03/bz/bz01a.html (creditors committee sought and obtained Chapter 11 trustee appointment). Alternatively, the committee may act beyond its statutory authority and expose the debtor's estate to potential losses. *See, e.g.*, Luedke v. Delta Airlines, Inc., 159 B.R. 385, 389–90 (S.D.N.Y. 1993) (alleging that the committee breached its fiduciary duty to plaintiffs through manipulative conduct during reorganization); *In re* 3DFX Interactive, Inc., No. 02–55795 JRG, 2006 Bankr. LEXIS 1498, at *8–10 (Bankr. N.D. Cal. June 29, 2006) (creditors' committee allegedly negotiated sale under proposed liquidating plan not in good faith and without involving U.S. trustee or other committee).

87. *See supra* notes 5–24 and accompanying text.

88. *See, e.g.*, *In re* Adelphia Commc'ns Corp., 386 B.R. 140, 147 (Bankr. S.D.N.Y. 2007) (explaining conflict and resulting years of delay in sale and plan process); *In re* Adelphia Commc'ns Corp., 345 B.R. 69, 73–74 (Bankr. S.D.N.Y. 2006) (same); David Peress & Thomas C. Prinzhorn, *Nontraditional Lenders and the Impact of Loan-to-Own Strategies on the Restructuring Process*, AM. BANKR. INST. J., Apr. 2006, at 48, 57–58 (discussing the dispute in

and the debtor, secured lenders, or other parties in interest—whether or not motivated by self-interest—can delay a case and affect value, such as in the Chapter 11 cases of *Brown Publishing*, *Chesapeake Corp.*, *Lyondell Chemical Co.*, *Six Flags*, *Stations Casino*, and *Tribune Co.*[89]

The potential for a committee or a few committee members to hijack or derail a debtor's restructuring efforts is troubling. It weakens the Chapter 11 process by eliminating one (and perhaps the most knowledgeable) check on the debtor's conduct and proposed reorganization plan—the bankruptcy court. Although the bankruptcy court oversees the Chapter 11 case and must approve any major transactions, the court ultimately must rely on the debtor and the creditors' committee for relevant information.[90] A self-interested committee can skew the court's and outside parties' perspectives of the

American Remanufacturers and noting that "[a]fter four days of confusing disputes about definitions of third parties, priming and subordination, the company lawyers informed the court that the company had run out of cash and converted to a chapter 7 liquidation"); Richman & Aberman, *supra* note 77, at 22, 60–63 (discussing conflicts and related issues raised in cases of *FiberMark*, *Galey & Lord* and *WorldCom*).

89. *See, e.g.*, Third Amended Disclosure Statement Accompanying Third Amended Joint Chapter 11 Plan of Reorganization for the LyondellBasell Debtors at 44–45, 53–56, *In re* Lyondell Chem. Co., No. 09–10023 (Bankr. S.D.N.Y. Mar. 12, 2010) (explaining litigation instituted by committee against debtors and certain lenders, the examiner's report finding no inappropriate conduct in connection with proposed plan that included providing equity to lenders and ultimate settlement of litigation); *see also* Emily Chasan, *Fight over What Six Flags Is Worth Could Get Ugly*, REUTERS, Dec. 3, 2009, http://www.reuters.com/article/2009/12/04/us-sixflags-idUSTRE5B30AR20091204 (explaining disputes among creditors, including creditors' committee, regarding valuation and control of reorganized debtor); Steve Green, *Station Casinos Reaches Deal with Key Lenders*, LAS VEGAS SUN, Feb. 25, 2010, *available at* http://www.lasvegassun.com/news/2010/feb/25/station-reaches-deal-key-lenders-hopes-emerge-bank/ (explaining dispute among the creditors' committee and other parties over control of reorganization process); Tom Hals, *Tribune's Creditors Warn of "World War" Legal Fight*, REUTERS, Feb. 12, 2010, http://www.reuters.com/article/idUSN1216183020100212 ("Tribune Co's senior creditors warned that allowing bondholders to sue over the legitimacy of $10 billion of the bankrupt company's debt would touch off 'World War III' and upend settlement talks, according to court documents."); Louis Lovio & John Reid Blackwell, *Sale OK'd Despite Protest*, RICHMOND TIMES DISPATCH, Mar. 24, 2009, at B7 (explaining creditors' committee's objections to debtor's sale process and noting that court rejected objections in approving sale); Ben Sutherly, *Brown Publishing, Creditors Clash Over Sale Plans*, DAYTON DAILY NEWS, June 27, 2010, at C1, *available at* http://www.daytondailynews.com/business/brown-publishing-creditors-clash-over-sale-plans-785011.html (committee objected to sale process in which secured lenders were credit bidding). Interestingly, most of these disputes concerned contests for control of the reorganized company or its value. The spouse of one of the authors is a lawyer in the corporate restructuring field and represented parties in the *Six Flags* and *Stations Casino* cases. Nonetheless, the authors' knowledge of, and all information in this Article regarding, these and other cases are based solely on the publicly available sources cited herein.

90. *See* Harner, *supra* note 48, Part III.B (discussing challenges faced by bankruptcy courts in resolving Chapter 11 cases based solely on information often strategically disclosed by the parties).

Chapter 11 case and foster a resolution that might not maximize value.

C. Prior Empirical Studies of the Chapter 11 Process

Several scholars have produced thoughtful empirical studies of the Chapter 11 process. These studies generally fall into one of five broad categories: adherence to the absolute priority rule;[91] corporate governance issues;[92] costs and expenses;[93] secured and debtor-in-

91. *See, e.g.*, Brian L. Betker, *Management's Incentives, Equity's Bargaining Power, and Deviations from Absolute Priority in Chapter 11 Bankruptcies*, 68 J. BUS. 161, 161 (1995) (explaining that the article will "examine[ ] the cross-sectional determinants of absolute priority deviations" in selected Chapter 11 bankruptcies); Julian R. Franks & Walter N. Torous, *An Empirical Investigation of U.S. Firms in Reorganization*, 44 J. FIN. 747, 748 (1989) (discussing the absolute priority rule and deviations from absolute priority).

92. *See, e.g.*, Douglas G. Baird & Edward R. Morrison, *Serial Entrepreneurs and Small Business Bankruptcies*, 105 COLUM. L. REV. 2310, 2368 (2005) ("Intelligent reform needs to be grounded . . . on the effects of Chapter 11 on entrepreneurs' career trajectories."); Catherine M. Daily & Dan R. Dalton, *Corporate Governance and the Bankrupt Firm: An Empirical Assessment*, 15 STRATEGIC MGMT. J. 643, 643–44 (1994) (examining the impact of the composition of a company's board of directors and board leadership structure on Chapter 11 filings); Catherine M. Daily, *Governance Patterns in Bankruptcy Reorganizations*, 17 STRATEGIC MGMT. J. 355, 356 (1996) (analyzing the effect of "audit committee composition and institutional investor holdings" on bankruptcy reorganizations); Jocelyn D. Evans & Corliss L. Green, *Marketing Strategy, Constituent Influence, and Resource Allocation: An Application of the Miles and Snow Typology to Closely Held Firms in Chapter 11 Bankruptcy*, 5011 J. BUS. RES. 225, 225–50 (2000) ("The objective of this study is to examine whether the managers' emphasis on marketing is related to the firms' likelihood of emerging from Chapter 11 as an independent entity."); Stuart C. Gilson & Michael R. Vetsuypens, *Creditor Control in Financially Distressed Firms: Empirical Evidence*, 72 WASH. U. L.Q. 1005, 1007 (1994) (examining creditor control in firms facing financial difficulties); M. Todd Henderson, *Paying CEOs in Bankruptcy: Executive Compensation When Agency Costs Are Low*, 101 NW. U. L. REV. 1543, 1594–618 (2007) (analyzing CEO compensation at financially troubled corporations); Lynn M. LoPucki & William C. Whitford, *Bargaining Over Equity's Share in the Bankruptcy Reorganization of Large, Publicly Held Companies*, 139 U. PA. L. REV. 124, 126 (1990) (finding a deviation from the absolute priority rule in an empirical analysis of Chapter 11 bankruptcies); Lynn M. LoPucki & William C. Whitford, *Compensating Unsecured Creditors for Extraordinary Bankruptcy Reorganization Risks*, 72 WASH. U. L.Q. 1133, 1146 (1994) (proposing a policy to "reduce the incentives for creditors to attempt to capture control of management"); LoPucki & Whitford, *supra* note 40, at 673 (analyzing the effect of creditor and shareholder influence over management on the value of financially distressed companies); Theresa J. Pulley Radwan, *Trustees in Trouble: Holding Bankruptcy Trustees Personally Liable for Professional Negligence*, 35 CONN. L. REV. 525, 525–27 (exploring the scope of the liability of bankruptcy trustees) (2003).

93. *See, e.g.*, STEPHEN J. LUBBEN, AM. BANKR. INST., CHAPTER 11 PROFESSIONAL FEE STUDY vi (2007) (analyzing professional fees in Chapter 11 bankruptcies); Edward I. Altman, *A Further Empirical Investigation of the Bankruptcy Cost Question*, 39 J. FIN. 1067, 1067 (1984) (assessing "both the direct and indirect costs of bankruptcy"); Brian L. Betker, *The Administrative Costs of Debt Restructurings: Some Recent Evidence*, FIN. MGMT., Winter 1997, at 56, 56; Avner Kalay et al., *Is Chapter 11 Costly?*, 84 J. FIN. ECON. 772, 795 (2007) ("Overall, our empirical evidence is inconsistent with the hypothesis that Chapter 11 results in net indirect costs."); Robert M. Lawless et al., *A Glimpse at Professional Fees and Other Direct Costs in Small Firm*

possession financing;[94] and overall effectiveness.[95] Notably, none of these studies focus on the intricacies of committee relations and operations in Chapter 11 and their potential impact on the process.

Nevertheless, some prior studies provide valuable insights regarding the committee's role in Chapter 11. This study in turn seeks to build on those observations and contribute an in-depth assessment of Chapter 11 committees to the literature. For example, in their study titled *Creditor Control and Conflict in Chapter 11*, Kenneth Ayotte and Edward Morrison analyze the extent and effect of creditor control and conflict in Chapter 11.[96] Their study is important for multiple reasons, including its empirical support for the increasing control

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Bankruptcies, 1994 U. ILL. L. REV. 847, 847 (analyzing "professional fees and direct costs in small firm bankruptcies").

94. *See, e.g.*, Kenneth M. Ayotte & Edward R. Morrison, *Creditor Control and Conflict in Chapter 11*, 1 J. LEGAL ANALYSIS 511, 513 (2009) (identifying the impact that creditor control and creditor conflict have on Chapter 11 bankruptcies of large corporations); Sris Chatterjee et al., *Debtor-in-Possession Financing*, 28 J. BANKING & FIN. 3097, 3098 (2004) (analyzing debtor-in-possession financing); Sandeep Dahiya et al., *Debtor-in-Possession Financing and Bankruptcy Resolution: Empirical Evidence*, 69 J. FIN. ECON. 259, 259 (2003) (analyzing whether debtor-in-possession financing produces overinvestment).

95. *See, e.g.*, Douglas G. Baird, *The New Face of Chapter 11*, 12 AM. BANKR. INST. L. REV. 69, 99 (2004) (summarizing the reasons why Chapter 11 bankruptcy has been particularly effective for large corporations); Baird & Morrison, *supra* note 92, at 2319 (examining the bankruptcy docket of one court during a single year); Samuel L. Bufford, *Chapter 11 Case Management and Delay Reduction: An Empirical Study*, 4 AM. BANKR. INST. L. REV. 85, 86 (1996) (analyzing the "fast track" method of bankruptcy case management and the resulting less delay it produces); Theodore Eisenberg & Lynn M. LoPucki, *Shopping for Judges: An Empirical Analysis of Venue Choice in Large Chapter 11 Reorganizations*, 84 CORNELL L. REV. 967, 969–71 (1999) (explaining the shift from New York to Delaware as the preferred choice of forums for adjudicating bankruptcy disputes); Jonathan C. Lipson, *Understanding Failure: Examiners and the Bankruptcy Reorganization of Large Public Companies*, 84 AM. BANKR. L.J. 1, 5–6 (2010) (analyzing factors that lead to the appointment of examiners in Chapter 11 cases); Lynn M. LoPucki, *The Debtor in Full Control—Systems Failure Under Chapter 11 of the Bankruptcy Code?*, 57 AM. BANKR. L.J. 99, 103 (1983) [hereinafter LoPucki, *Debtor I*] (analyzing the effect of lack of creditor control in Chapter 11 cases in the Western District of Missouri); Lynn M. LoPucki, *The Debtor in Full Control—Systems Failure Under Chapter 11 of the Bankruptcy Code?*, 57 AM. BANKR. L.J. 247, 247 (1983) [hereinafter LoPucki, *Debtor II*] (same); Wilbur N. Moulton & Howard Thomas, *Bankruptcy as a Deliberate Strategy: Theoretical Considerations and Empirical Evidence*, 14 STRATEGIC MGMT. J. 125, 125 (1993) (discussing reasons for the continued use bankruptcies despite their high cost); Elizabeth Warren & Jay Lawrence Westbrook, *The Success of Chapter 11: A Challenge to the Critics*, 107 MICH. L. REV. 603, 603 (2009) (responding to critics of Chapter 11 bankruptcies and arguing that it is an effective tool); Douglas Baird et al., *The Dynamics of Large and Small Chapter 11 Cases: An Empirical Study* 33 (Yale ICF, Working Paper No. 05–29, 2007), *available at* http://papers.ssrn .com/sol3/papers.cfm?abstract_id=866865 ("The cold reality is that Chapter 11 does nothing or close to nothing for ordinary general creditors in the typical small business bankruptcy."); Stephen J. Lubben, *Chapter 11 "Failure"* 3 (Seton Hall Pub. Law, Research Paper No. 1375163, 2009), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1375163 (empirically describing why firms fail in Chapter 11 bankruptcies).

96. Ayotte & Morrison, *supra* note 94, at 511.

exercised by creditors in Chapter 11, which represents a shift from the more traditional notion of debtor or shareholder influence over Chapter 11.[97] They also collect and analyze data regarding objections filed by creditors' committees and conclude that "[t]hese [unsecured creditors' committee] objections suggest strongly that, in a large number of cases, the managers of the corporation are not acting to maximize the returns of unsecured creditors, who are often the firm's residual claimants."[98]

A study by Lynn LoPucki, titled *The Debtor in Full Control—Systems Failure Under Chapter 11 of the Bankruptcy Code?*, takes a different perspective on Chapter 11 in a different time period, but also considers committee activity in the process.[99] The LoPucki study was performed shortly after the enactment of the Bankruptcy Code and provides early empirical insight regarding the use of creditors' committees under Chapter 11 of the Bankruptcy Code. It posits that "[c]reditors' committees were appointed in only 40% of cases, fewer than half of these committees employed counsel, and in general the committees were ineffective."[100] It also analyzes potential causes of committee ineffectiveness and suggests that lack of incentives, unqualified members, committee form, and member geographic dispersion may contribute to the problem.[101]

Likewise, in an updated analysis of business failures in Chapter 11, Stephen Lubben presents data explaining factors that predict the likelihood of a Chapter 11 case being converted to a case under Chapter 7 of the Bankruptcy Code or dismissed.[102] The study invokes a thoughtful regression model to identify and eliminate potential causes of business failure (defined as conversion or dismissal) in Chapter 11.[103] The study concludes, among other things,

97. *See id.* at 538 ("Creditors dictate the dynamics of the reorganization process.").

98. *Id.* at 526. According to the study, "[j]unior creditors, acting through a creditors' committee, filed objections in more than 50 percent of the cases." *Id.* at 514.

99. *See* LoPucki, *Debtor I*, *supra* note 95, at 100 (discussing the frequency with which creditors' committees are used in Chapter 11 bankruptcies); LoPucki, *Debtor II*, *supra* note 95, at 249–53 (discussing the role of creditors' committees under the Bankruptcy Code).

100. LoPucki *Debtor I*, *supra* note 95, at 100.

101. LoPucki *Debtor II*, *supra* note 95, at 251–52; *see also* Eklund & Roberts, *supra* note 77, at 129 ("[A creditor's] acceptance of an active participatory role in a bankruptcy proceeding through service on a committee is most likely motivated by each committee member's interest in obtaining the maximum possible return on its claim."); Catherine E. Vance & Paige Barr, *The Facts & Fiction of Bankruptcy Reform*, 1 DEPAUL BUS. & COM. L.J. 361, 389 (2003) (suggesting similar factors as limiting effectiveness of committees).

102. *See* Lubben, *supra* note 95, at 3–5 (outlining the factor that can cause Chapter 11 bankruptcies to fail).

103. *See id.* at 7–9 (describing the regression model and the variables used).

that the appointment of a committee suggests creditor interest in the case and, consequently, a lower probability that the case will fail.[104]

The study in this Article takes these and similar important findings regarding various aspects of committees in Chapter 11 and presents the first comprehensive analysis of committee work. The study recognizes and accounts for the numerous factors that may impact a Chapter 11 case. Its findings also are supplemented by survey data collected from Chapter 11 professionals and former committee members to incorporate off-docket influences—for example, events and personal dynamics not included in motions, objections, and other pleadings filed on the court's docket. The authors devoted significant attention to the design and analysis of the study to generate an accurate and complete as possible picture of a committee's role in Chapter 11. The details of the study's methodology and primary findings are explained in the next Part.

III. STUDY METHODOLOGY

The study's primary objective is to provide data on the function of creditors' committees in Chapter 11 cases and assess, among other things, how creditors' committees impact value allocation among the debtor's various stakeholders. The study's design reflects this objective, collecting data from a cross-section of business bankruptcy cases in three primary and three supplemental jurisdictions (the case database). In addition, the authors conducted a separate survey study of 600 individuals who either served as a committee member or as a professional in one or more of the Chapter 11 cases included in the case database.[105] The survey data are presented in a separate study, but are also referenced in this Article as applicable.[106] The following discussion explains the components of the case database and the general design and scope of the study.

104. *Id.* at 14.

105. Specifically, once the case database was completed, the authors and coders identified counsel to the debtor and any creditors' committee and any committee members in each of the cases in the database. The Bureau then randomly selected 300 professionals and 300 committee members for inclusion in the survey database. The Bureau also made every reasonable effort to verify contact information for these individuals.

106. 252 professionals and 212 committee members were contacted and met eligibility criteria. Ultimately, 77 (30.7%) professionals and 48 (22.5%) committee members participated in the survey. Both are valid response rates for these types of surveys.

A. The Case Database

The case database consists of 296 Chapter 11 cases filed during 2002–2008.[107] This time period captures the end of the previous economic downturn, the prosperity of the mid-2000s, and the beginning of the most recent economic downturn. Accordingly, it provides data that are representative of different points of the economic cycle. The case database contains information about each of these cases from the date of the filing of the case through the case being closed by the court or June 30, 2009, whichever is earlier, with certain supplements through June 30, 2010.[108]

Many large business bankruptcy cases are filed in the District of Delaware and the Southern District of New York.[109] The study collects data from each of these jurisdictions, as well as the Northern District of Illinois (which has a more moderate business bankruptcy filing rate), for each of the years included in the study.[110] In addition, the study includes Chapter 11 cases filed in three additional jurisdictions—the Central District of California, the District of Maryland, and the Northern District of Ohio—for the years 2004 and 2006.[111] The data from the additional jurisdictions provide further

107. The case database includes one case filed in 2001. This case was the lead case in the Chapter 11 cases of the lead debtor and its affiliates. One of the affiliate debtors filed its case in 2002 and was selected for the database through the stratified random selection process. Consistent with the study's methodology, the lead case was substituted for the eliminated affiliate case. The authors considered replacing this case but elected to retain it for consistency purposes and because it was filed only five months before the study period.

108. For cases coded as "unresolved" as of June 30, 2009, the authors performed additional analyses to incorporate data from the docket regarding any sales, plans of reorganization or liquidation or other resolutions recorded between June 30, 2009 and June 30, 2010. As of June 30, 2010, only 12 of the 296 cases in the database are coded as unresolved.

109. The case database includes approximately 10% of all qualifying Chapter 11 cases filed in the Southern District of New York during the study period and approximately 26% of all qualifying Chapter 11 cases filed in the District of Delaware during the study period. Appendix A describes the process for identifying qualifying Chapter 11 cases.

110. The case database includes approximately 23% of all qualifying Chapter 11 cases filed in the Northern District of Illinois during the study period. Appendix A describes the process for identifying qualifying Chapter 11 cases.

111. The case database includes approximately 16% of all qualifying Chapter 11 cases filed in the Northern District of California during the study period, 32% of all qualifying Chapter 11 cases filed in the District of Maryland during the study period, and approximately 44% of all qualifying Chapter 11 cases filed in the Northern District of Ohio during the study period. Appendix A describes the process for identifying qualifying Chapter 11 cases. The years 2004 and 2006 were selected to collect data from these additional jurisdictions in time periods both before and after the October 17, 2005 general effective date of certain amendments to the Bankruptcy Code. *See* Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109–8, § 436(b), 119 Stat. 23, 113 (2005) (discussing changes in the law regarding "Duties in Small Business Cases").

diversity in the types of case filings. As a result, the study evaluates data from jurisdictions in six different federal judicial circuits.[112]

Given the authors' desire to test meaningful differences between jurisdictions and over time, the authors used a stratified random sample. Specifically, the population of eligible Chapter 11 business cases was segregated into groups by jurisdiction and by year filed. The sample was then selected from each group using equal probability sampling.[113] Also, given the authors' desire to test meaningful differences within committee cases and then between committee and noncommittee cases, the case database was supplemented with a stratified random sample from the LoPucki Business Bankruptcy Project ("BBP") database using the same criteria.[114] The authors used this approach because a majority of BBP cases involve committees.

Based on these general guidelines, and as further explained in Appendix A, 296 cases were selected for the case database. The authors believe that the final case database represents a meaningful cross-section of Chapter 11 cases filed in the United States between 2002 and 2008.

B. The Study's Design and Scope

The authors also devoted significant time to creating, testing, revising, and finalizing the project code book. Specifically, the authors developed an initial code book and tested it on three Chapter 11 cases. They then distributed the code book to three other coders, reviewed it with them, and revised it based on their feedback. The authors and coders tested the code book by coding numerous practice cases. After this coding exercise, the team met with the Bureau of Sociological Research (the "Bureau") to review the test coding results. The authors revised the code book based on the results and follow-up conversations

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112. The selected jurisdictions represent the Second Circuit, Third Circuit, Fourth Circuit, Sixth Circuit, Seventh Circuit, and Ninth Circuit.

113. The authors worked with the Bureau to determine a sample size that would provide accurate and reliable data. The sample size of 296 cases generally corresponds with a confidence interval of 5 and a confidence level of 95%. The sample size and the selection of the overall population itself also were determined based in part on the budget for this project.

114. Lynn M. LoPucki, UCLA School of Law, Bankruptcy Research Database, http://lopucki.law.ucla.edu/bankruptcy_research.asp (last visited Feb. 3, 2011). Specifically, the Bureau randomly selected 26 cases from the BBP, which represent 18% of the 146 cases in the BBP population. This percentage corresponds to that reflected in the initial database of 270 cases, which is approximately 18% of the total 1,499 cases in the overall population. The coders for this study then collected all of the data for those cases from the courts' dockets in accordance with the codebook and procedures applicable to the other cases included in the case database.

with the Bureau and coders. This process was repeated four times, resulting in a final code book consisting of 129 primary variables and an acceptable level of intercoder reliability.[115]

The primary variables included in the code book cover the following general categories: general case information; general committee information; committee activity; committee conflict; allocation of ownership interests through plan or sale; general creditor recoveries; and miscellaneous creditor information. The variables within each category then identified specific information, such as the pleading type, the filing party, and the ultimate resolution. Coders thoroughly researched each case in the database assigned to them by using PACER to identify, pull, and read documents relevant to the coding variables. Accordingly, data entered in the database reflect information on the court docket.

Upon completion of the coding process, the authors, with the assistance of the Bureau, reviewed and reconciled any inconsistencies in the case database. This process required only minor changes throughout the database. The authors then commenced their analyses of the data.

IV. KEY DATA PRESENTATION AND ANALYSIS

As discussed in Part II, cases and scholarship suggest that creditors are asserting more control in Chapter 11 cases.[116] Creditors are obtaining this control in a variety of ways, including through covenants in contracts with the debtor and purchasing sizable claims against the debtor's bankruptcy estate. Creditors also appear to be vying for and using appointments to creditors' committees to obtain information regarding, and leverage over, debtors.[117] Such conduct could alter significantly the committee's motivation and role in

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115. The primary variables were broken down further into sub-variables to remove subjective judgment from the coding process. In addition, the Bureau designed and monitored a web-based entry system to reduce coder error throughout the process. Coders also double-coded cases to insure intercoder reliability during the actual study.

116. *See supra* Part II.B; *see also* Douglas G. Baird & Robert K. Rasmussen, *Private Debt and the Missing Lever of Corporate Governance*, 154 U. PA. L. REV. 1209, 1237–42 (2006) (explaining increased creditor control exercised through financing contracts); David A. Skeel, *Creditors' Ball: The "New" New Corporate Governance in Chapter 11*, 152 U. PA. L. REV. 917, 918, 923–27 (2003) ("Whereas the debtor and its managers seemed to dominate bankruptcy only a few years ago, Chapter 11 now has a distinctively creditor-oriented cast."). The foregoing sources are cited and the issues are discussed in Harner, *supra* note 48. Interestingly, approximately one-third of individuals responding to the professionals and committee member surveys observed an increase in creditor control in Chapter 11 cases.

117. The potential consequences of increased creditor control are discussed in Harner, *supra* note 48; *see also* Ayer et al., *supra* note 78 (discussing survey data).

Chapter 11 cases, as well as the value of the bankruptcy estate and ultimate returns to stakeholders.

Based on the legislative history to Chapter 11 of the Bankruptcy Code and the contemplated role of creditors' committees,[118] this study proposes the following hypothesis:

Hypothesis No. 1: Creditors' committees add value to Chapter 11 cases, as determined by returns to unsecured creditors and company reorganizations.

Based on anecdotal evidence from Chapter 11 cases,[119] this study also proposes the following hypothesis:

Hypothesis No. 2: The presence or absence of conflict or self-interest in the composition of creditors' committees impacts value in Chapter 11 cases, as determined by returns to unsecured creditors and company reorganizations.

The study collected a wealth of information regarding committees in Chapter 11 cases. The depth of this information helped the authors better understand the general functioning of committees and, in turn, enhanced their analysis of the data and the primary hypotheses. This Part first presents key background data to provide context for the overall study. It then explains how the data were analyzed based on case characteristics, including the presence of a committee, the type of committee, and the results of the Chapter 11 case. The Part concludes by presenting data necessary to test the two primary hypotheses. Although sample sizes are insufficient to determine statistically whether any overall effects hold within each jurisdiction, jurisdictions with observed patterns that differ from the reported overall effect are mentioned in footnotes.

A. General Case Information

The Chapter 11 cases included in the case database reflect the full range of potential Chapter 11 business debtors.[120] Of the 296 cases, 85.5 percent involved debtors organized as corporations, 1.4 percent involved partnerships, one percent involved limited

118. *See supra* Part II.A.

119. *See supra* Part II.B.

120. As discussed *supra* Part III.A, the cases were systematically collected from six jurisdictions. Accordingly, 29.4% of the cases were filed in the District of Delaware, 24.3% were filed in the Northern District of Illinois, 25.3% were filed in the Southern District of New York, 6.8% were filed in the District of Maryland, 6.8% were filed in the Central District of California, 6.8% were filed in the Northern District of Ohio, and 0.7% were filed in the Southern District of New York but subsequently transferred to another jurisdiction.

partnerships, 11.1 percent involved limited liability companies, and one percent were unknown. The majority of debtors were private businesses, with twenty-five percent of the debtors identifying themselves as public companies. In addition, 16.2 percent of the cases were small business cases and 7.4 percent involved single asset real estate debtors.[121]

The debtors operated in a variety of industries, with a concentrated number operating in manufacturing (19.3 percent); transportation, communications, electric, gas, and sanitary services (12.8 percent); wholesale or retail trade (14.2 percent); finance, insurance, and real estate (17.2 percent); and services (29.1 percent).[122] Information collected from the debtors' schedules of assets and liabilities indicate that the mean and median assets were $903,250,000 and $2,508,000, respectively, and the mean and median liabilities were $248,910,000 and $6,156,700, respectively.[123] In addition, the debtors' statements of financial affairs showed a mean and median of $177,170,000 and $1,040,300, respectively, as the gross annual income in the last full year preceding the Chapter 11 petition.[124]

According to debtors' Chapter 11 petitions, 65.9 percent of the cases involved between 1–199 creditors, 12.8 percent involved 200–999

121. Certain provisions of the Bankruptcy Code applicable to small business debtors changed as a result of the 2005 amendments to the Bankruptcy Code. Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109–8, § 436(b), 119 Stat. 23, 113 (2005). Among other things, the definition of "small business debtor" in Section 101(51D) of the Bankruptcy Code was amended such that a debtor ceases to be a small business debtor if the U.S. trustee appoints a creditors' committee in the case. 11 U.S.C. § 101(51D) (2006). To ascertain whether this amendment affected the data, the authors analyzed the small business debtor cases filed before and after October 17, 2005. That data are as follows: Prior to October 17, 2005, there were 17 (85%) NC cases, 3 (15%) UCC cases, and 0 OC cases involving a debtor coded as a small business debtor. On or after October 17, 2005, there were 25 (89.3%) NC cases, 2 (7.1%) UCC cases, and 1 (3.6%) OC case involving a debtor coded as a small business debtor. Although cell sizes were insufficient to perform an impact analysis, the descriptive data suggest little variation in the two time periods.

122. Other industries represented in the database include agriculture, forestry, and fishing (0.7%); mining (0.7%); and construction (3.0%).

123. For consistency purposes, if a Chapter 11 case involved more than one debtor (that is, the debtor's case was jointly administered with its affiliate debtors' cases), coders used information listed in the lead debtor's schedules of assets and liabilities. Accordingly, if the lead debtor did not file consolidated schedules, the coded data might not reflect the full amount of assets or liabilities. The large difference between the mean and median values is a reflection of the influence of a few companies with extremely large assets or liabilities on the mean.

124. For consistency purposes, if a Chapter 11 case involved more than one debtor (that is, the debtor's case was jointly administered with its affiliate debtors' cases), coders used information listed in the lead debtor's statement of financial affairs. Accordingly, if the lead debtor did not file a consolidated statement, the coded data might not reflect the full amount of gross income.

creditors, 19.6 percent involved 1,000 or more creditors, and 1.7 percent involved an unknown number of creditors. A Chapter 11 trustee was appointed to replace the debtor's management in only 2.7 percent of the cases, and an examiner was appointed in only 3.4 percent of the cases. As of the close of the data on June 30, 2010, only 4.1 percent of the cases remained pending with no resolution to the debtor's reorganization efforts (that is, no plan or sale of substantially all assets). Table 1 sets forth the resolution of the 296 cases included in the dataset.[125]

Table 1: Case Resolution

	Frequency (%)
Plan of reorganization confirmed	117 (39.5)
Plan of liquidation (or liquidating plan of reorganization) confirmed	77 (26.0)
Case dismissed	72 (24.3)
Sales with no confirmed plan or conversion	13 (4.4)
Case still pending with no ultimate resolution	12 (4.1)
Sale of debtor's assets in chapter 11 case with no subsequent plan and then conversion to chapter 7	2 (0.7)
Case transferred to another jurisdiction	2 (0.7)
Conversion to case to chapter 7 prior to sale of debtor's assets and/or plan confirmation	1 (0.3)
Total	296 (100.0)

B. General Committee Information

The cases in the database not only provide a representative sample of business debtors, but also provide a fairly equal sampling of cases in which a creditors' committee was appointed under section 1102 of the Bankruptcy Code (creditors' committees) and cases in

125. The focus of the study was not case resolution but rather the impact, if any, of creditors' committees on case resolution. Accordingly, Table 1 describes the outcomes of the cases included in the database as a point of reference. These data may reflect the forum and case parameters used in creating the database and thus should be used with caution in relation to studies focusing solely on case outcome based on different parameters.

which a committee was not appointed. Specifically, 143 cases (48.3 percent) involved at least one creditors' committee and 153 cases (51.7 percent) involved no creditors' committees.[126] Of the cases with creditors' committees, 95.8 percent had one creditors' committee, 2.1 percent had two creditors' committees, and 2.1 percent had three creditors' committees.[127]

The database also includes information about statutory committees of equity holders (equity committees) and ad hoc committees of creditors or equity holders (ad hoc committees).[128] Although not the focus of the study, an active equity committee or ad hoc committee can alter the dynamics of the Chapter 11 case. The study captures relevant information to, among other things, control for those factors. These data show equity committees in 2.7 percent of the cases and active ad hoc committees in 11.1 percent of the cases.[129]

Although not by design, the database provided two very strong, natural comparative categories of data—data for cases with no committees and data for cases with committees.[130] The analysis set forth below divides these data one step further, with three comparative categories emerging: cases with no committees ("NC"); cases with only one creditors' committee ("UCC");[131] and cases with multiple committees or a committee other than a creditors' committee ("OC"). A case with multiple committees may, for example, have two official committees of creditors representing different types of creditors' claims or a creditors' committee and an official committee of equity holders.[132] These categories result in 144 NC cases, 115 UCC

126. Overall, 152 cases (51.4%) involved some type of committee (that is, creditors' committee, equity committee, ad hoc committee, or some combination), leaving 144 cases (48.6%) with no committee involvement.

127. Of the cases with creditors' committees in the database, the types of creditors' committees include general unsecured creditors (98.6%), banks and other financial institutions (0.7%), personal injury claimants (2.1%), employees or retirees (2.8%), and other claimants (2.1%).

128. *See, e.g.*, Jonathan C. Lipson, *The Shadow Bankruptcy System*, 89 B.U. L. REV. 1609, 1671–72 (discussing use of ad hoc committees to influence Chapter 11 cases and the issues created by that practice).

129. The cases with ad hoc committees break down as follows: 63.6% involve one ad hoc committee, 15.1% involve two ad hoc committees, and 21.2% involve three ad hoc committees.

130. The authors elected to use three categories because the dynamics and, consequently, results can be significantly different in cases involving just one creditors' committee versus cases involving multiple creditors' committees or different types of committees.

131. The abbreviation "UCC" frequently is used as a shorthand reference for "unsecured creditors' committee" in the Chapter 11 context. Accordingly, that abbreviation is used to identify the category capturing data for cases involving only one official "unsecured creditors' committee."

132. For a discussion of the multiple committee structure, see *supra* note 63 and accompanying text.

cases, and thirty-seven OC cases.[133] The phrase "committee type" as used herein refers to these three comparative categories. Appendix B sets forth the descriptive information for each of the categories, including size and types of business debtors, number of creditors, and the filing jurisdictions.

C. Committee Activity

A business debtor typically uses Chapter 11 to restructure through a plan of reorganization or a sale of substantially all of its assets.[134] A debtor also may use a plan to sell its assets or to distribute the proceeds of sales to stakeholders.[135] These plans are referred to as liquidating plans or plans of liquidation.

When a business files a Chapter 11 case, the U.S. trustee may appoint a creditors' committee to monitor the debtor and work to increase returns to creditors.[136] The creditors' committee may try to achieve the latter objective through negotiating a favorable plan of reorganization or encouraging a debtor to sell its assets on a piecemeal or going concern basis. This Article examines the influence of creditors' committees on these critical restructuring decisions in Parts IV.C.1 and C.2, respectively. It then considers two questions directly related to the first hypothesis: Does the presence of a creditors' committee facilitate a reorganization of the debtor's business and increase returns to the debtor's creditors? Part IV.D presents data addressing the frequency and impact of conflicts and litigation on a

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133. In the OC case category, 8 cases have only ad hoc committees, 1 case has only an equity committee, and 28 cases have some combination of committees. In certain instances, the small sample size of this category did not allow for robust analyses, and those analyses focus on the NC cases and UCC cases.

134. *See* 11 U.S.C. § 363(b) (2006) (explaining sale process); *id.* § 1125 (listing requirements for content of plan); *id.* § 1129 (detailing requirements for confirmation of plan).

135. A debtor who sells its assets in Chapter 11 has three primary options for completing its restructuring efforts:

> Chapter 11 debtors have traditionally chosen among three possible courses of action after a sale of their assets. First, a debtor could proceed with confirmation of a liquidating chapter 11 plan, which requires compliance with §§ 1123 and 1129. . . . Second, a debtor could convert the chapter 11 case to a case under chapter 7 and allow a chapter 7 trustee to distribute a debtor's remaining assets, if any, to creditors and to prosecute any available avoidance actions. Third, a debtor could seek entry of a simple order dismissing the chapter 11 case, returning the parties to their state law rights and remedies.

Norman L. Pernick & G. David Dean, *Structured Chapter 11 Dismissals: A Viable and Growing Alternative After Asset Sales*, AM. BANKR. INST. J., June 2010, at 1, 55–56; *see also* A. Joseph Warburton, *Understanding the Bankruptcies of Chrysler and General Motors: A Primer*, 60 SYRACUSE L. REV. 531, 539–41 (2010) (explaining the advantages of pursuing a section 363 sale rather than a sale under a plan).

136. *See supra* Part II.A.3.

debtor's Chapter 11 case, which is the focus of the second hypothesis. Finally, the Article tests the hypotheses based on the foregoing data analyses in Part V.E.

1. The Plan Process

The Bankruptcy Code sets forth the requirements for confirming (that is, obtaining court approval of) a plan of reorganization or liquidation.[137] Among other things, section 1129 requires that the plan comply with the provisions of the Bankruptcy Code, be proposed in good faith, make disclosures regarding payments under the plan, and be accepted by at least one class of impaired claims.[138] A claim is considered impaired unless the plan "leaves unaltered the legal, equitable, and contractual rights to which such claim . . . entitles the holder."[139] Holders of impaired claims and interests under the proposed plan typically are entitled to vote on whether to accept or reject the plan.[140]

A debtor may start negotiating its plan with key stakeholders prior to the filing of the bankruptcy case. If the debtor achieves a consensus on a plan during this prepetition period, the case usually involves a prepackaged or pre-arranged plan, and it proceeds quicker than a free-fall (that is, no prenegotiated plan) case.[141] Otherwise, a debtor will negotiate its plan during the course of the Chapter 11 case with its stakeholders, including any creditors' or equity committees. Ad hoc committees also may get a seat at the negotiating table.[142]

The Bankruptcy Code provides the debtor with an exclusive period to file and solicit votes on its plan for the first 120 and 180 days of the case, respectively.[143] Under amendments to the Bankruptcy Code implemented in 2005, the bankruptcy court may extend the

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137. § 1129 (detailing requirements for confirmation of plan).

138. *Id.*

139. *Id.* § 1124(1) (explaining impairment of claims and interests under plan).

140. *Id.* § 1126 (explaining voting procedures relating to Chapter 11 plans). Under section 1126, holders of unimpaired claims and interests are deemed to accept the plan, and holders of claims and interests who do not receive any distributions under the plan are deemed to reject it. *Id.* § 1126(f)–(g).

141. *See, e.g.*, John D. Ayer et al., *Out-of-Court Workouts, Prepacks and Pre-Arranged Cases: A Primer*, AM. BANKR. INST. J., Apr. 2005, at 16, 16–17 (discussing details of prepackaged and pre-arranged Chapter 11 cases); *see also* § 1125(g) (allowing a debtor to solicit acceptance of a plan prior to filing its Chapter 11 petition under certain circumstances).

142. *See, e.g.*, Carrianne Basler & Michelle Campbell, *Savvy Claims Purchasers Must Avoid Pitfalls*, AM. BANKR. INST. J., June 2006, at 26, 26 (explaining use of ad hoc committee to participate in plan negotiations).

143. § 1121(d) (setting forth deadlines relating to the filing and solicitation of acceptances of plan).

debtor's exclusivity period for not more than eighteen and twenty months, respectively, from the petition date.[144] This amendment altered prior practice, which allowed bankruptcy courts to continue to extend the debtor's exclusive periods for cause indefinitely.[145]

Analysis of the case database reveals that the plan process differs among the three committee types. First, this Section considers the overall case duration and the duration between the case filing and plan confirmation. Second, it discusses creditors' committee and noncommittee objections to the debtor's plans.

a. Case Duration

Of the 296 cases in the database, the debtor filed a plan in 236 of the cases—109 NC cases, ninety UCC cases, and thirty-seven OC cases. The bankruptcy court confirmed plans in 199 of these cases. Although, overall, NC cases are significantly shorter in duration than UCC cases ($p=.001$), no significant differences emerged among the three categories with respect to the time elapsing between the filing of the case and confirmation of a plan.[146]

Table 2: Predicted Case Durations (in days)

	Filing of Case to Case Closure	**Filing of Case to Plan Confirmation**
NC	699	424
UCC	1193	472
OC	1076	482

144. NC cases are significantly less likely than UCC cases ($p < .001$) and OC cases ($p < .001$) to have more than one request by the debtor to extend its exclusive periods under section 1121.

145. *See, e.g.*, Jeffrey M. Schlerf, *BAPCPA's Impact on Exclusivity is Hard to Gauge*, J. CORP. RENEWAL, July 1, 2007, *available at* http://www.turnaround.org/Publications/Articles.aspx?objectID=7797 (explaining possibility of unlimited extensions of exclusivity prior to the amendments to the Bankruptcy Code and observing that "[m]ost courts routinely granted an initial extension in the early stages of a case and were inclined to grant further extensions if a debtor demonstrated that it was making sufficient progress in the formulation of a Chapter 11 plan").

146. Analysis based on negative binomial regressions. Overall case duration was calculated from the petition date (filing of the case) through the date that the case was closed. Only 189 of the 296 cases have been officially closed by order of the bankruptcy court. Accordingly, this analysis is based on 189 cases. This pattern is not observed in the Central District of California, where the average duration for the 11 NC cases is 1,111 days and the average duration for the 3 UCC cases is 998. In addition, no significant difference emerged in overall duration with respect to the OC cases, which may be due to insufficient power.

b. Objections to Plan

Creditors' committees rarely filed objections or pleadings relating to the debtor's plan. As discussed above, a creditors' committee is empowered by the Bankruptcy Code to engage with the debtor in plan negotiations.[147] Bankruptcy court dockets typically do not reflect negotiations, but parties may file objections or other pleadings in the Chapter 11 case to obtain leverage in the negotiations. Interestingly, creditors' committees filed one or more objections or pleadings relating to the debtor's plan in only fourteen cases. This finding corresponds to prior studies suggesting a lack of meaningful activity by creditors' committees in Chapter 11 cases.[148] The finding does not reflect off-docket activity, however, and as such, it should be considered in light of other findings regarding case resolution and creditors' recoveries.[149]

Moreover, when analyzing committee objections in the UCC case and OC case categories, OC cases are significantly more likely to have a plan objection filed by the creditors' committee than UCC cases ($p=.019$).[150] This finding corresponds to the notion that committees use formal objections to achieve greater bargaining power in negotiations, which may be more contentious in cases involving multiple committees.

The appointment or appearance of one or more committees in a case likely reflects increased creditor interest in the case. The plan objection data support this. For example, OC cases are significantly more likely than NC cases ($p<.001$) and UCC cases ($p=.001$) to have plan objections filed by stakeholders other than a committee.[151]

147. *See* § 1103(c) (listing powers of statutory committees); *see also supra* Part II.A.

148. *See supra* Part II.C.

149. *See infra* Parts IV.C.3–4 (discussing findings on reorganization as compared to liquidation and on the effects of committees on unsecured creditors).

150. Analysis based on logistic regression. Furthermore, this pattern is observed in all forums. Although sample size did not permit separate analysis, equity committees filed plan objections in 4 of the 8 cases with a plan and an equity committee. Ad hoc committees filed plan objections in 12 of the 33 cases with a plan and an ad hoc committee.

151. This pattern is not observed in the Central District of California where UCC cases are more likely than OC cases to have such a plan. OC cases also are significantly more likely than UCC cases ($p = .006$) and NC cases ($p = .021$) to involve a prepackaged or pre-arranged plan. This pattern is not observed in the District of Delaware where a greater percentage of NC cases involve a prepacked or pre-arranged plan than do OC cases; however, a greater percentage of OC cases involve a prepackaged or pre-arranged plan than do UCC cases. This pattern is also not observed in the Northern District of Illinois where a greater percentage of NC cases involve such a plan than UCC and OC cases; there is no difference between UCC and OC cases in that jurisdiction.

Likewise, UCC cases are significantly more likely than NC cases ($p=.008$) to have noncommittee plan objections.[152]

2. The Sale Process

Section 363(b) of the Bankruptcy Code permits a debtor, after notice and a hearing, to "use, sell, or lease, other than in the ordinary course of business, property of the estate."[153] Debtors invoke this section to sell a portion or substantially all of their assets to a third party. Purchasers often are enticed to buy a debtor's assets in bankruptcy because section 363(f) permits the debtor to sell its assets under certain specified circumstances free and clear of all claims, liens, or encumbrances asserted against the debtor or its assets.[154] Some practitioners and commentators have suggested that debtors no longer reorganize under Chapter 11; rather, they simply use the process to sell assets under the special protections of section 363 of the Bankruptcy Code.[155]

Analysis of the case database reveals that the sale process differs among the three committee types. The following analysis considers motions to sell assets (including whether an auction process was used), objections to the sale motions, and ultimate approvals of the sale motions.

a. Motions to Sell Assets

Debtors filed motions to sell substantially all of their assets in ninety-nine of the 296 cases in the database—twenty-seven NC cases, sixty-seven UCC cases, and five OC cases. UCC cases are significantly more likely than NC cases ($p<.001$) and OC cases ($p<.001$) to involve a

152. This pattern is observed in all forums.

153. 11 U.S.C. § 363(b) (2006) (setting forth requirements for sales outside the ordinary course of business).

154. *Id.* § 363(f) (authorizing sales "free and clear of any interest in such property" if one of five conditions is met). For a thoughtful exploration of section 363(f) and an argument that it is applied too broadly, see George W. Kuney, *Misinterpreting Bankruptcy Code Section 363(f) and Undermining the Chapter 11 Process*, 76 AM. BANKR. L.J. 235 (2002).

155. *See, e.g.*, Douglas G. Baird & Robert K. Rasmussen, *The End of Bankruptcy*, 55 STAN. L. REV. 751, 751–52 (2002) (discussing the trend of resolving Chapter 11 cases through the sale, rather than plan, process and increased creditor control in that context); *see also* Kuney, *supra* note 154, at 272 ("The courts' inclusion of 'claims' within 'interests' under § 363(f) and the erosion of the bias against preplan sales of substantial groups of assets has led to the use of Chapter 11 to achieve a prenegotiated sale of a business or group of assets and to protect the buyer from successor liability."); Harvey R. Miller & Shai Y. Waisman, *Is Chapter 11 Bankrupt?*, 47 B.C. L. REV. 129, 129 (2005) (discussing the trend and similar issues).

motion to sell substantially all of the debtor's assets.[156] This finding may suggest that active creditors' committees encourage a sale rather than reorganization of the debtor's business in Chapter 11. It would be consistent with observed trends regarding increased activity by distressed debt investors, both on committees and in their individual capacities, who typically have short-term objectives and investment horizons. Because this finding may have significant import for Chapter 11 policy, it is analyzed further below in connection with liquidating plans and the parties participating in the Chapter 11 case.[157]

b. Auction Process

Although not technically required by section 363, debtors may use an auction process to market and sell their assets.[158] An auction process can help ensure that the debtor receives the best or highest offer for the assets.[159] UCC cases are significantly more likely to involve an auction process than NC cases (p=.003).[160]

156. Analysis based on logistic regression. This pattern is not observed in the District of Maryland where 1 of the 7 (14.3%) UCC cases has a filed motion while 4 of 13 (30.8%) of NC cases has a filed motion.

157. *See infra* Part IV.C.3.

158. Section 363(b) technically requires only "notice and a hearing." § 363(b); *see also* FED. R. BANKR. P. 2002 (setting forth notice and disclosure requirements in the context of a sale). In general, a bankruptcy court will approve the section 363(b) sale if the debtor demonstrates sound business justifications for the sale. *See, e.g.*, *In re* Chrysler LLC, 576 F.3d 108, 117–18 (2d Cir. 2009) (explaining that "the sale of an asset of the estate under § 363(b) is permissible if the 'judge determining [the] §363(b) application expressly find[s] from the evidence presented before [him or her] at the hearing [that there is] a good business reason to grant such an application' ") (quoting *In re* Iridium Operating LLC, 478 F.3d 452, 466 (2d Cir. 2007)); *see also* Stephens Indus., Inc. v. Mallory Co., Inc., 789 F.2d 386, 390 (6th Cir. 1986) (explaining standard); Comm. of Equity Sec. Holders v. Lionel Corp. (*In re* Lionel Corp.), 722 F.2d 1063, 1071 (2d Cir. 1983) ("The rule we adopt requires that a judge determining a § 363(b) application expressly find from the evidence presented before him at the hearing a good business reason to grant such an application."); *In re* Montgomery Ward, 242 B.R. 147, 153–54 (D. Del. 1999) (listing factors to be considered in determination).

159. *See, e.g.*, Marshall Huebner & Rajesh James, *Duties and Obligations of Officers and Directors in § 363 Sales*, AM. BANKR. INST. J., Dec. 2009/Jan. 2010, at 36, 36 ("[O]nce the decision has been made to sell discrete assets or the enterprise under § 363, the debtor's obligation is to maximize the estate's value by soliciting and accepting the 'highest and best' available bid.").

160. This pattern is not observed in the District of Delaware where 29 of 35 (82.9%) of UCC cases involve an auction process and 3 of 3 (100%) of NC cases involve an auction process. Similarly, this pattern is not observed in the Northern District of Ohio where 4 of 5 (80%) of UCC cases involve an auction process and 2 of 2 (100%) of NC cases involve an auction process. Finally, this pattern is also not observed in the District of Maryland where 0 of 1 (zero percent) of UCC cases and 1 of 4 (twenty-five percent) of NC cases involve such a process.

c. Objections to Sale Motions

Similar to the plan process, a committee may use an objection to a proposed sale to affect negotiations with the debtor or the potential purchaser. Of the seventy-one cases involving a sale motion and a creditors' committee, the committee filed objections or other pleadings relating to the sale in only nineteen of the cases.[161] UCC cases are significantly more likely than NC cases (p=.016), however, to have sale objections filed by noncommittee parties, again indicating increased stakeholder activity in committee cases.[162] As discussed above, the lack of committee activity represented by these findings must be considered in connection with other findings and the survey data collected from Chapter 11 professionals and committee members.[163]

No significant differences emerged in whether the court ultimately approved the sale motion, but the duration between the filing of the sale motion and approval of the sale is significantly longer in NC cases as compared to UCC cases (p=.026).[164] The bankruptcy court may take more time to consider and approve sales in NC cases because there is no formal oversight by a committee and typically no auction process.[165] Debtors in NC cases also may require more time to negotiate on an individual basis with all key stakeholders.[166] Nevertheless, because many NC cases have a concentrated group of creditors (or even a single large creditor), the shorter duration of sales in UCC cases may result from pressure by the stakeholders, including the committee in some cases, to consummate a sale quickly.[167]

161. Ad hoc committees filed sale objections in 3 of the 5 cases with a sale and an ad hoc committee. No cases involved a sale motion and an equity committee.

162. This pattern is not observed in the District of Maryland where the 1 UCC case had no such objections and 3 of the 4 (75%) NC cases did have such an objection. This pattern is not observed in the Central District of California where 2 of the 3 (66.7%) UCC cases involved such an objection and all 3 of the NC cases (100%) did involve such an objection.

163. *See supra* Part IV.C.1.

164. This pattern is not observed in the Southern District of New York where the average duration of NC cases is 30.33 days and the average duration for UCC cases is 33.80 days.

165. *See* data *supra* note 160 for approval of an auction process in NC cases; *see also* Warburton, *supra* note 135, at 559 (positing that "courts are reluctant to disturb a sale at auction, [which makes] the adoption of the bidding procedures . . . strategically important").

166. *See, e.g.*, Baird & Bris, *supra* note 95, at 25 ("The need to resolve tax obligations is the engine that drives the typical small chapter 11 case.").

167. For example, some commentators have complained that the quick sales requested in the *General Motors* and *Chrysler* cases were facilitated by pressure from certain creditors. *See, e.g.*, John Blakeley, *Lehman, Chrysler, GM: The Fallout,* DEAL MAG., Aug. 7, 2009, *available at* http://www.thedeal.com/magazine/ID/029091/features/lehman,-chrysler,-gm-the-fallout.php ("'In GM, the need for speed was contrived in order to oppress creditor rights. And absent some

3. Reorganization Versus Liquidation

The two preceding Sections focus on whether a debtor reorganizes its business or sells its assets in the Chapter 11 case and a creditors' committee's role in that decisionmaking process.[168] This analysis captures only part of the story. Further analysis into the ultimate resolution of the Chapter 11 case is necessary to test the first hypothesis. That analysis follows and will help determine if UCC cases are likely to foster more overall liquidations or simply more section 363 sales, as indicated in Part IV.B.2.

a. Impact of Committee on Case Resolution

Overall, the bankruptcy courts confirmed plans of reorganization in 60.3 percent of the cases and plans of liquidation in 39.7 percent of the cases in the database with confirmed plans.[169] The predicted probabilities that NC cases, UCC cases, and OC cases would have a confirmed plan of liquidation (rather than a confirmed plan of reorganization) are .29, .63, and .14, respectively. Accordingly, UCC cases are significantly more likely than NC cases ($p<.001$) and OC cases ($p<.001$) to involve a confirmed plan of liquidation.[170]

b. Potential Confounding Factors

The preference for liquidations over reorganizations may not stem solely from the desires or conduct of creditors' committees. Other factors, such as the size of the case, the number of creditors, and the involvement of any secured creditors, also may influence that result. To that end, candidate control variables included number of creditors, approval of DIP financing, assets, liabilities, and secured claims. Due to the nature of the coding scheme, number of creditors was dichotomized to differentiate between cases with zero to forty-nine

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clarification of [Section] 363, this could always be the case.' " (quoting counsel to a group of GM bondholders)).

168. *See supra* Part IV.C.2.

169. This analysis includes 194 confirmed plans, which differs slightly from the total of 199 confirmed plans used to consider the duration of cases from filing to confirmation in Part IV.C.1 above. This difference results from the exclusion of five cases that were dismissed after confirmation of the plan because of the debtor's nonpayment or other defaults on postconfirmation obligations. These five cases represent the only postconfirmation dismissals in the database.

170. This pattern is not observed in the District of Maryland where 2 of the 6 (33.3%) UCC cases involve a confirmed plan of liquidation while 3 of the 6 (50%) NC cases involve a confirmed plan of reorganization.

creditors and cases with fifty or more creditors[171] Assets, liabilities, and secured claims were dichotomized based on each variable's median. The meaning of such categorization reflects the effect of being above or below the median on assets, liabilities, or secured claims. Following Hosmer and Lemeshow's model-building strategies, candidate control variables were included in the final multivariate model when they had a bivariate relationship with the outcome variable (here, liquidation versus reorganization) at the p=.25 significance level.[172] All candidate control variables, with the exception of number of creditors, met this criterion; however, assets, liabilities, and secured claims were highly correlated and thus only the asset category was retained. In a model controlling for DIP financing and assets, the effect remained significant.[173]

4. Creditors' Recoveries

The dual goals of Chapter 11 are rehabilitation and maximizing returns to creditors.[174] The discussion above focuses on the rehabilitation versus liquidation objective. This Section considers returns to unsecured creditors and whether a committee affects the amount of those returns, which again informs analysis of the first hypothesis.[175]

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171. Number of creditors was measured using an eleven-point scale with ten category ranges (for example, 1–49, 50–99, 100–199) and an "unknown" category. This dichotomy was selected because it most closely approximates this variable's median. Of the 291 cases reporting number of creditors, 45% (n = 131) reported 99 or fewer creditors while the remaining 55% (n = 161) reported 50 or more creditors.

172. DAVID W. HOSMER & STANLEY LEMESHOW, APPLIED LOGISTIC REGRESSION (2d ed. 2000).

173. *See infra* Appendix C, Table 2. Also, as discussed previously, "committee type" refers to the categories of no committee (NC cases), single creditors' committee (UCC cases) and multiple or other committee cases (OC cases) used for comparative purposes. *See supra* Part IV.B. In the database, 194 cases involve a plan of reorganization or liquidation of which 189 have information on all covariates. Therefore, these analyses are based on 189 cases.

174. *See* H.R. REP. NO. 95–595, at 220 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6179 ("The purpose of a business reorganization case [under Chapter 11] . . . is to restructure a business's finances so that it may continue to operate, provide its employees with jobs, pay its creditors, and produce a return for its stockholders."); S. REP. NO. 95–989, at 10 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5787, 5796 (discussing dual goals of legislation); *see also* Toibb v. Radloff, 501 U.S. 157, 163–64 (1991) (discussing traditional dual goals of Chapter 11); Warren, *supra* note 40, at 340 (same).

175. The phrase "general unsecured creditors" refers to creditors classified as "general unsecured" under the plan or distribution order filed in the debtor's case. This class typically represents the beneficiaries of the creditors' committee. Coders also were instructed to code separately information for other classes of unsecured creditors. The analyses in this Part discuss results based on all coded categories of unsecured creditors. This approach provided a broader

Creditors' committees and their members are fiduciaries for creditors holding unsecured claims.[176] Accordingly, their conduct in the Chapter 11 case should aim to increase the percentage recovery received by unsecured creditors. Admittedly, a variety of factors may influence creditor returns. Nevertheless, regression analyses provide meaningful insight into committees' impact on creditors' recoveries.

Analysis of the case database reveals differences in recoveries among committee types and between plan confirmation types. First, this Section considers the return to creditors in all cases. Second, it discusses the return to creditors in UCC cases only. Again, a variety of case characteristics apart from committee type may influence creditors' recoveries and thus this Section also presents multivariate analyses.

a. All Cases

Of the 296 cases, 238 cases have valid information for percentage recoveries to unsecured creditors.[177] The data show the following overall returns to unsecured creditors: 1.7 percent of the cases had no recovery; 0.7 percent had less than one percent recovery; 14.9 percent had one to ten percent recovery; 8.4 percent had eleven to twenty-five percent recovery; 5.1 percent had twenty-six to fifty percent recovery; 2.7 percent had fifty-one to seventy-five percent recovery; and 22.6 percent had seventy-six to one hundred percent recovery. An analysis of the median percentage recovery for unsecured creditors reveals that unsecured creditors in half of the cases in the case database received twenty-five percent or less of their claim value and unsecured creditors in the other half received more than twenty-five percent of their claim value.

To analyze creditors' recoveries by categories, the data were collapsed into two percentage groups—creditors receiving distributions equal to fifty percent or less of their claim and those receiving more than fifty percent. Unsecured creditors in UCC cases are significantly *less* likely than those in NC cases (p=.007) and OC

perspective on the treatment of unsecured creditors in the cases. Nevertheless, similar results emerged based on analyses of the general unsecured creditors class.

176. *See supra* Part II.A.3.

177. Coders were instructed to record the percentage recovery listed in the debtor's disclosure statement or the distribution order for, among others, the class of general unsecured creditors. The 58 cases without valid information for this variable involve cases that did not reflect this information on the docket, including cases that were dismissed or converted prior to any plan or distribution order. In addition, in 72 cases, the disclosure statement or other disclosure of recoveries to unsecured creditors listed the percentage recovery as "unknown." Accordingly, the analyses are based on the 166 cases with known percentage recoveries.

cases ($p \leq .001$) to receive a distribution representing more than fifty percent of their claims.[178] There is a marginally significant difference between NC and OC cases ($p=.004$). In a model controlling for DIP financing and assets, the effects remained the same with the exception of the marginal difference between NC and OC cases which disappeared ($p=.634$).[179]

The finding that unsecured creditors do better in OC cases than in UCC cases corresponds with the notion that there is more value, and thus more to fight about, in cases involving more than one committee. Those cases tend to be larger in overall size and affected creditors.[180] In addition, equity committees typically are appointed only if there is some suggestion that the debtor's enterprise value is sufficient to pay all creditors in full and thus leave some value for shareholders.[181] Nevertheless, the data suggest that creditors might benefit if parties were more open to multiple committees in the appropriate Chapter 11 cases.[182]

b. UCC Cases Only

Focusing solely on the UCC cases, unsecured creditors are significantly ($p<.001$) more likely to receive larger percentage

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178. Analysis based on logistic regression. This pattern is not observed in the District of Maryland where 1 of the 3 (33.3%) of the UCC cases receive a distribution representing more than 50% of their claim, while 0 of the 3 (0%) NC cases receive a distribution representing more than 50% of their claim. In the database, 166 cases have information on percentage recovery to unsecured creditors of which 162 have information on all covariates. Therefore, these analyses are based on 162 cases.

179. *See supra* Part IV.C.3; *see also infra* Appendix C, Table 1.

180. *See* Kurt F. Gwynne, *Intra-committee Conflicts, Multiple Creditors' Committees, Altering Committee Membership and Other Alternatives for Ensuring Adequate Representation Under Section 1102 of the Bankruptcy Code*, 14 AM. BANKR. INST. L. REV. 109, 115–18 (2006) (discussing the factors relevant to the appointment of multiple committees).

181. *See id.* at 134 ("One of the main factors in decisions refusing to order the appointment of an additional committee is the expense associated with the additional committee.").

182. Consider the following observation:

> Thus, despite the legislative history that seems to encourage the appointment of multiple committees in large cases, "Bankruptcy Courts generally have been reluctant to [order the appointment of] separate committees of unsecured creditors notwithstanding the diverse and sometimes conflicting interest of such creditors in the context of a Chapter 11 proceeding." This is particularly troublesome where creditors on the committee have not only different financial motivations, but also claims entitled to different legal priorities. For example, employee claims might be entitled to priority under Bankruptcy Code section 507(a)(3), whereas nonpecuniary loss penalty claims might be subordinated.

Klee & Shaffer, *supra* note 2, at 1025 (citations omitted). *But see* Gwynne, *supra* note 180, at 134–35 (discussing costs associated with multiple committees). Parties must weigh the costs (including conflicts) and benefits to multiple committees, as intracommittee litigation was filed in 25 of the database cases.

distributions (that is, distributions in excess of fifty percent) in reorganization cases as opposed to liquidation cases.[183] This finding suggests that reorganization cases hold more value for unsecured creditors. The data show the same finding for unsecured creditors in all cases.[184]

D. Conflicts and Litigation Involving Committees

As suggested in the discussion of multiple committees above, increased creditor activity in Chapter 11 cases may be beneficial, but it also presents certain risks. For example, conflicts can develop either pre- or postpetition among various creditors or creditor groups, and creditors' engagement in the process may result in self-dealing behavior. This Section considers the prevalence of creditors' committee conflicts in Chapter 11 cases and the impact of those conflicts on entity value. These data inform the analysis of the second hypothesis.

1. Potential Conflicts

Detecting potential conflicts of interest in Chapter 11 cases can be challenging. Other than the debtor and certain professionals, most parties in interest have no obligation to disclose their relationships with, various claims against, or interests in the debtor, its insiders, or its competitors.[185] Consequently, the parties and their pleadings often

183. This analysis is based on 52 cases with a confirmed plan or approved sale motion, a known percentage payment and one creditors' committee. This pattern is not observed in the Southern District of New York where 40% of both reorganizing and liquidating cases result in a percentage distribution exceeding 50% (there are 5 cases in each category).

184. Of the 138 cases with a confirmed plan or approved sale motion and a known percentage payment, 65.2% involved plans of reorganization and 34.8% involved liquidation. The data show creditors in 56.7% of reorganizations receiving greater than 50% and receiving the same level of distribution in only 29.2% of the liquidation cases. Thus, there is a significant effect of plan type such that reorganizations are significantly more likely than liquidations ($p = .002$) to receive distributions in excess of 50%. Furthermore, this pattern is observed in all forums. For example:

> The premise of the Railroad Equity Receiverships—that a reorganized financial entity will realize more value as a going concern than through its liquidation—has remained unchanged despite four extensive amendments to the Bankruptcy Reform Act and a comprehensive review of the operation of the Bankruptcy Reform Act by the National Bankruptcy Commission appointed in 1996.

Harvey R. Miller & Shai Y. Waisman, *Does Chapter 11 Reorganization Remain a Viable Option for Distressed Businesses for the Twenty-First Century?*, 78 AM. BANKR. L.J. 153, 190 (2004).

185. *See, e.g.*, 11 U.S.C. § 327 (2006) (discussing professionals in bankruptcy cases); *id.* § 1107 (discussing debtors in possession); FED. R. BANKR. P. 1007 (outlining debtor's financial and other disclosure obligations); *id.* r. 2016 (discussing disclosures for professionals seeking compensation in case); *id.* r. 2019 (discussing lawyers representing multiple parties in interest); *see also supra* Part II.A.3. The scope of disclosures under Bankruptcy Rule 2019 is often

fail to detect many conflicts in the Chapter 11 case. The data results are limited in this respect, as they only reflect conflicts or potential conflicts that were discernible from the docket. The data thus are likely underinclusive.

Nevertheless, at least one member of the creditors' committee held some interest or asserted some position that presented a potential conflict in thirty-five percent of the database cases with creditors' committees. The U.S. trustee and the bankruptcy courts confronted some of the conflicts on a regular basis and typically deemed them not detrimental to a party's service on the committee.[186] Examples of these conflicts include indenture trustees and parties to contracts and leases with the debtor. Some of the conflicts were more unique, however, and raise concerns. Examples of these conflicts include members who held both secured and unsecured debt, held both equity and unsecured debt, or were controlled by alleged insiders of the debtor.

2. Litigation by Committee Members and the Committee

Disputes and resulting litigation also can represent a conflict of interest or an agenda different than general unsecured creditors or the other members of the creditors' committee. This type of activity can signify creditor interest in the debtor's restructuring, which Congress sought to increase in structuring the Bankruptcy Code to benefit all stakeholders in the Chapter 11 process. Accordingly, the study evaluated key pleadings filed in the Chapter 11 case by creditors' committees and their members.

In some cases, members of the creditors' committee did not rely on the committee to file pleadings representative of its position. For example, individual committee members filed objections to: the proposed DIP financing in fifteen cases (fifteen percent of creditors' committee cases with a filed DIP motion); the sale motion in nineteen cases (twenty-seven percent of creditors' committee cases with a filed sale motion); the disclosure statement in fifteen cases (thirteen percent of creditors' committee cases with a filed disclosure statement); and the plan in twelve cases (ten percent of creditors'

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contested, particularly in the context of a lawyer representing an ad hoc committee. *See, e.g.*, George R. Mesires, *Continued Uncertainty over Rule 2019 May Chill Participation of Distressed Investors*, AM. BANKR. INST. J., Mar. 2010, at 1, 1 (explaining debate concerning Rule 2019 and split among bankruptcy court decisions).

186. *See* Gwynne, *supra* note 180, at 120–29 (discussing types and treatment of committee members' conflicts).

committee cases with a filed plan).[187] The data show that individual members are significantly more likely to file an objection to a plan ($p<.001$) when the committee also files an objection.[188]

One or more committees also filed objections and pleadings in relation to activities by key players in the Chapter 11 cases, in addition to those committee objections discussed in Part IV.C. Among others, committees filed an objection to the secured creditors' prepetition claims in 43.4 percent of the database cases involving creditors' committees.[189] Moreover, they filed an objection or other pleading opposing the debtor's conduct in sixty-seven percent of the database cases involving creditors' committees.[190] The latter finding lends some support to the role of the committee as a statutory watchdog or supervisor of the debtor's conduct.[191]

3. Impact of Conflicts and Litigation on Value

Conflicts and competition are innate to the Chapter 11 process—a process designed to aggregate and resolve, often by compromising a party's position, all claims and interests asserted against a debtor's limited pool of resources. The goal should not be eliminating conflicts and competition; rather, the focus should be on aligning these characteristics with value maximization. This goal

187. Some cases involved more than one type of objection by individual members. Overall, 98 cases (68% of creditors' committee cases) did not involve an individual creditors' committee member objection to the proposed DIP financing, sale motion, disclosure statement or plan.

188. Individuals filed objections to the plan in 7 of the 104 (6.7%) cases in which committees did not file an objection and in 5 of the 14 (35.7%) cases in which committees did file an objection. The effect is significant ($p < .001$), indicating that individuals are *more* likely to file an objection to the plan when the committee also files an objection to the plan. Individuals filed objections to the DIP motion in 5 of the 46 (10.9%) cases in which committees did not file an objection and in 10 of the 51 (19.6%) cases in which committees did file an objection. The effect is not significant ($p = .235$), indicating that whether or not individuals file an objection to the DIP motion does not depend on whether or not the committee files an objection. Individuals filed objections to the sale motion in 15 of the 52 (28.8%) cases in which committees did not file an objection and in 4 of the 19 (21.1%) cases in which committees did file an objection. The effect is not significant ($p = .511$), indicating that whether or not individuals file an objection to the sale motion does not depend on whether or not the committee files an objection. Individuals filed objections to the disclosure statement in 10 of the 92 (10.9%) cases in which committees did not file an objection and in 5 of the 23 (21.7%) cases in which committees did file an objection. The effect is not significant ($p = .166$), indicating that whether or not individuals file an objection to the disclosure statement does not depend on whether or not the committee files an objection. Interpret results with some caution due to one insufficient cell size. Also, this pattern is observed in all forums.

189. Committees filed an objection to the secured creditors' prepetition claims in 41% of UCC cases.

190. Committees filed an objection or other pleading opposing the debtor's conduct in 60% of UCC cases.

191. *See supra* Part II.A.3.

requires an understanding of the impact of the various potential conflicts and disputes recorded in the database.

Interestingly, analysis of the case database reveals that neither the presence of conflict nor litigation has a significant effect on whether a debtor reorganizes or liquidates[192] or on the percentage recovery received by general unsecured creditors.[193] Cases with these characteristics do, however, evidence adverse consequences for the estate and the debtor's stakeholders. For example, the estate incurred significantly greater costs relating to committees' professional fees and expenses in cases involving conflicts of interest by a member of the creditors' committee or committee litigation against secured lenders or the debtor.[194] Moreover, cases involving committee

192. A conflicting interest was held by at least one creditors' committee member in 44 of the 104 cases involving creditors' committees and plans of reorganization or liquidation; 51.7% of cases with no conflict involved plans of liquidation, while 43.2% of cases with a conflict involved plans of liquidation. There is no significant effect of conflicting interest on whether the debtor confirms plan of reorganization or liquidates ($p = .392$). Committee litigation against secured creditors occurred in 22 cases; 37.8% of cases with no such litigation involved plans of liquidation while 54.5% of cases with litigation involved plans of liquidation. There is no significant effect of litigation on whether the debtor confirms plan of reorganization or liquidates ($p = .130$). Committee litigation against the debtor occurred in 77 cases; 35.2% of cases with no such litigation involved plans of liquidation while 47.2% of cases with litigation involved plans of liquidation. There is no significant effect of litigation on whether the debtor confirms plan of reorganization or liquidates ($p = .100$).

193. Of the 82 cases with a creditors' committee and information about percentage recoveries to general unsecured creditors, 25% of cases with a creditors' committee and no conflict provided distributions to general unsecured creditors in excess of 50%, while 34.2% of cases with a conflict provided like distributions. There is no significant effect of conflicting interest on whether or not the payment percentage exceeds 50% ($p = .361$). Similarly, 42.6% of cases with no creditors' committee litigation against secured creditors provided distributions to general unsecured creditors in excess of 50%, while 33.3% of cases with such litigation provided like distributions. There is no significant effect of litigation on whether or not the payment percentage exceeds 50% ($p = .315$). Finally, 45.4% of cases with no creditors' committee litigation against the debtor provided distributions to general unsecured creditors in excess of 50%, while 31.6% of cases with such litigation provided like distributions. There is no significant effect of conflicting interest on whether or not the payment percentage exceeds 50% ($p = .086$).

194. Of cases with at least one creditors' committee and a committee member conflict, 103 included information about committees' professional fees and expenses. Forty-three (41.7%) of these cases involved conflicting interest, while 60 (58.3%) did not. The predicted total costs of cases with and without conflicting interest are $9,655,131 and $1,126,921, respectively. There is a significant effect of conflicting interest on total cost such that cases with a conflicting interest have a significantly greater total cost than cases with no conflicting interest ($p < .001$). This pattern is observed in all forums. Of cases involving any committee litigation against secured creditors, 106 included information about committees' professional fees and expenses. Forty-eight (45.3%) of these cases involved litigation against secured creditors while 58 (54.7%) did not. The predicted total costs of cases with and without such litigation are $7,145,548 and $2,540,827, respectively. There is a significant effect of litigation against secured creditors on total cost such that cases with litigation against secured creditors have a significantly greater total cost than cases with no such litigation ($p < .001$). This pattern is not observed in the District of Delaware, the Central District of California or the Northern District of Ohio where cases with no such

litigation against the debtor are significantly longer than cases without such litigation (p=.011).[195]

Overall, the data suggest that conflicts of interest and litigation involving creditors' committees are expensive distractions but otherwise do not impact entity value.[196] It certainly is plausible that the effects of known conflicts and disputes are neutralized by their public disclosure. Armed with information regarding conflicts and disputes, parties can take appropriate steps to protect their interests. The problem, if any, may be the unknown or nonpublic influences and disputes.

In this respect, the absence of a strong association between conflicts or litigation and certain outcomes in the Chapter 11 case focuses the analysis of the creditors' committee role. If conflicts or litigation do not affect value, what characteristics of the committee structure might contribute to the findings in Part IV.C? Part V explores this question and proposes possible explanations and solutions.

E. Testing the Hypotheses

The data provide valuable insights into the operation of Chapter 11 cases and the conduct of creditors' committees. The descriptive data help explain what is occurring in Chapter 11 cases, and the various regression analyses help predict what might occur in

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litigation result in greater costs than cases with such litigation. Of cases involving any committee litigation against the debtor, 106 included information about committees' professional fees and expenses. Seventy-eight (73.6%) of these cases involved litigation against the debtor while 28 (26.4%) did not. The predicted total costs of cases with and without such litigation are $5,980,412 and $843,234, respectively. There is a significant effect of litigation against the debtor on total cost such that cases with such litigation have a significantly greater total cost than cases with no such litigation ($p < .001$).

195. Of cases involving any committee litigation against the debtor, 187 included case duration information (i.e., time elapsed between petition date and date case closed). One hundred forty-five (77.5%) of these cases did not involve such litigation while 42 (22.5%) did involve such litigation. The predicted durations of cases with and without such litigation are 1,240 days and 794 days, respectively. There is a significant effect of litigation against the debtor on case duration (petition to close) such that cases with such litigation are significantly longer than cases without such litigation ($p = .011$). This pattern is observed in all forums. These analyses did not include the two cases in the database that were transferred to a jurisdiction not included in the study.

196. The most popular related responses to the professionals and committee member surveys indicate that conflicts either increase or do not impact the amount of creditors' recoveries, with more respondents perceiving increases.

future cases. As discussed below, the data also lend support for rejecting the primary hypotheses.[197]

It is important to note that cases were not randomly assigned to a particular committee type (for example, no committee, one creditors' committee only, some combination of committees); rather, it is likely (and probably certainly) the case that the various committee types were attracted to cases with a certain set of characteristics. For example, cases with few assets may not attract any committee activity. As mentioned previously, this selection effect (of committee types to cases) was addressed by considering a variety of control variables in the key analyses testing the first hypothesis.[198] In theory, it is difficult to account for all possible confounding variables because it may be the case that the substantive literature has yet to define them. That being said, substantively relevant confounds that were included in the coding scheme were thoroughly examined. Future research may identify and control for other potential confounds not addressed here.

1. Hypothesis No. 1: Committees Add Value

This hypothesis asserts that creditors' committees add value to Chapter 11 cases, as determined by returns to unsecured creditors and company reorganizations. As discussed in Part IV.C, the data show that UCC cases are significantly less likely than NC cases and OC cases to provide returns to unsecured creditors in excess of fifty percent.[199] Moreover, UCC cases are significantly more likely than NC cases and OC cases to resolve through a liquidation, rather than reorganization, of the debtor.[200] As such, the data tend to support rejecting the hypothesis.

As discussed in Part V, creditors' committees may add value to cases not reflected on the docket or in the data. For example, a twenty-five percent recovery is better than a ten percent recovery, and the committee might be responsible for creating or extracting that value for unsecured creditors. The data do, however, provide reason to

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197. The authors recognize the limitations on the data results due to, among other things, off-docket activity and certain information not being available for all cases on the dockets. Nevertheless, the authors have scrutinized the data and believe that it provides not only useful information for courts, policymakers, and practitioners, but that it also supports some of the anecdotal evidence discussed in this Article. The authors do not, however, assert that the findings prove or disprove any observations.

198. *See supra* Part IV.C.3.

199. *See supra* Part IV.C.4.

200. *See supra* Part IV.C.3.

evaluate further the roles of committees, particularly in the context of Chapter 11 liquidations.

2. Hypothesis No. 2: Conflicts and Self-Dealing Impact Value

This hypothesis asserts that the presence or absence of conflict or self-interest in the composition of creditors' committees impacts value in Chapter 11 cases, as determined by returns to unsecured creditors and company reorganizations. As discussed in Part IV.D, the data suggest that potential conflicts of interest of individual committee members do not affect either the debtor's reorganization efforts or general unsecured creditors' percentage recoveries.[201] The same finding emerged for litigation instituted by the creditors' committee against secured creditors and debtors.[202] As such, the data tend to support rejecting the hypothesis.

As discussed in Part V, these findings do not necessarily mean that the identity of committee members or their conduct is irrelevant to the analysis. Rather, they encourage a more meaningful evaluation of the committee structure and the nature of disclosures in Chapter 11. If the presence of a creditors' committee may increase the likelihood of liquidation, as suggested in Part IV.C, the analysis needs to focus on factors other than known conflicts and disputes. Part V examines potential contributing factors and proposes some solutions to mitigate any value impact.

V. REFLECTIONS ON DATA AND IMPLICATIONS FOR CHAPTER 11 POLICY

Creditors need representation in the Chapter 11 process. The Bankruptcy Code facilitates this representation through creditors' committees.[203] Those committees are not used in every case, however, and may encourage more liquidations and lower distributions to general unsecured creditors.[204] The latter finding is somewhat counterintuitive and deserves further analysis. This Part dissects what is known about creditors' committees from Part IV, additional data in the study, and anecdotal evidence, and it proposes that explanations may lie in the composition of the committee and the circumstances of the particular cases.

201. *See supra* Part IV.D.3.
202. *See supra* Part IV.D.3.
203. *See supra* Part II.A.3.
204. *See supra* Parts IV.B, IV.C.3–4.

A. Creditors' Committees and Liquidation

Chapter 11 cases involving either a sale of substantially all of the debtor's assets or liquidation typically reach resolution quicker than reorganizations.[205] The data also suggest that most creditors receive lower distributions in liquidations than in reorganizations.[206] Nevertheless, from a creditor's perspective, the prospect of quicker resolution may outweigh a potential increase in recovery.

It is difficult to discern creditor preferences from Chapter 11 dockets, but the data offer important clues. For example, many creditors' committees include financial institutions—indenture trustees, bondholders, and unsecured lenders—in their membership.[207] Financial institutions often hold large unsecured claims against the debtor, have the resources to participate in the Chapter 11 case, and qualify to serve on the creditors' committee. In many cases, these parties can lend expertise and context to committee deliberations and decisions. They may also hold a different perspective than other committee members, however, on the debtor's reorganization options.

Anecdotal evidence suggests that financial institutions no longer engage in relationship lending and often prefer a quick liquidation of a troubled credit.[208] These tendencies may be enhanced if the financial institution is a hedge fund or the institution's proprietary trading division, which typically possess short-term

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205. The predicted durations for cases involving liquidation plans or sales and reorganization plans are 131 days and 196 days, respectively. There are significant differences in duration such that cases with a liquidation plan or sale resolve more quickly than do cases that reorganize ($p = .002$). This pattern is not observed in the District of Delaware where the average duration for reorganizing cases is 113 days and the average duration for liquidating cases is 150 days.

206. In comparing cases involving plans of reorganization against those involving plans of liquidation or sale motions, creditors received more than 50% in 56.7% of the reorganization cases and 27.8% of the liquidation cases. The difference is significant ($p = .001$). The same result emerges if the comparison is limited solely to plans of reorganization versus plans of liquidation ($p = .002$).

207. In the case database, 143 cases involve at least one creditors' committee. All 143 cases have information about whether or not financial member served on the creditors' committee. Of these cases, 59 (41.3%) had at least one financial institution on the creditors' committee while the remaining 84 (58.7%) did not. Moreover, of the 143 cases, 76 (53.1%) resulted in liquidation (or sale motion), 54 (37.8%) resulted in reorganization, and 13 (9.1%) had some other resolution.

208. *See, e.g.*, Harner, *supra* note 48, at 110–11 (discussing increased syndication and selling of loan positions and breakdown in relationship lending); *see also* Frederick Tung, *Leverage in the Board Room: The Unsung Influence of Private Lenders in Corporate Governance*, 57 UCLA L. REV. 115, 117 (2009) (exploring the dynamics of lending relationships in corporate governance).

investment horizons.[209] Moreover, short-term investors may have hedged their claims against the debtor, thereby limiting their financial exposure, or they may have purchased their claims at a significant discount.[210] These and other similar preferences do not necessarily represent conflicts of interest and may not be discernible from the docket, but they certainly may affect how those members influence and vote on committee decisions.

Interestingly, the data indicate that cases with at least one financial institution serving on the creditors' committee at some point during the case were significantly more likely to result in reorganization (as opposed to liquidation) than were cases with no financial institution members.[211] This result could support several alternative, and meaningful, inferences. For example, financial institutions could be seeking positions on the committee to facilitate a debt-for-equity exchange and ownership in the reorganized company.[212] Alternatively, the presence of a different voice—for example, a financial institution rather than all trade creditors—may generate more thorough discussions regarding the debtor's restructuring alternatives.[213] Moreover, creditors' committees may benefit from the expertise of financial institution members in their review of proposals by, and discussions with, the debtor. This result remained even after controlling for factors such as asset size, number

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209. *See, e.g.*, Michelle M. Harner, *Trends in Distressed Debt Investing: An Empirical Study of Investors' Objectives*, 16 AM. BANKR. INST. L. REV. 69, 102–03 (2008) (setting forth empirical data regarding creditors' investment horizons and objectives).

210. *See, e.g*, Jonathan C. Lipson, *The Shadow Bankruptcy System*, 89 B.U. L. REV. 1609, 1662 (2008) (explaining investment and hedging strategies of hedge funds and similar investors in Chapter 11 process); Robert K. Rasmussen, *Where Are All the Transnational Bankruptcies? The Puzzling Case for Universalism*, 32 BROOK. J. INT'L L. 983, 1001–02 (2007) (discussing involvement and objectives of hedge funds and similar investors in Chapter 11 process).

211. Of the 130 cases with a creditors' committee that result in either liquidation or reorganization, 76 (58.5%) result in liquidation (including sale motion) and 54 (41.5%) result in reorganization. Furthermore, of these 130 cases, 56 (43.1%) have at least one financial member on the creditors' committee and 74 (56.9%) do not. The predicted probabilities that a case with at least one financial member and a case with no financial members will liquidate are .446 and .689, respectively. There is a significant effect of whether or not a financial member is on the creditors' committee such that cases not involving a financial member are significantly more likely than cases involving a financial member to liquidate (including sale motions) than to reorganize ($p = .005$). This pattern is observed in all forums. The presence of a financial institution on a creditors' committee did not significantly affect percentage recoveries to general unsecured creditors.

212. *See* Harner, *supra* note 209, at 82–87 (reporting results of a survey showing that certain investors target the debt of troubled companies to facilitate a debt-for-equity exchange or otherwise acquire equity interests in the company).

213. *See infra* Part V.B.

of creditors, presence of secured debt, and approval of DIP financing.[214]

Committee member turnover also may allow one or more longer-term members (whether or not financial institutions) to assert more influence over the process. One or more committee members resigned or were removed from creditors' committees in twenty-five percent of database cases involving creditors' committees.[215] Accordingly, instability in committee composition may contribute to certain member preferences having more sway in any given case.

In addition, there are potentially relevant differences between UCC cases, which tend to liquidate more frequently, and NC and OC cases, which tend to reorganize.[216] For example, NC cases generally involve a small number of creditors and limited assets and, as a result, increased owner/management control over the outcome.[217] Owners and managers will pursue reorganization to, among other things, salvage their investment in and employment with the debtor. NC cases also may arise in the prepackaged or pre-arranged plan context where quick implementation of a plan of reorganization typically is the primary goal.[218]

Likewise, as discussed in Part IV.C, OC cases tend to involve a greater number of claims asserted against a larger pool of assets, with more creditors' interests represented in the process.[219] The first attribute suggests that there may be more value to distribute and realize through reorganization. The second attribute suggests that more checks exist on debtor, secured creditor, and creditors' committee conduct. Consequently, it may be more difficult for any one creditor to influence the outcome of the Chapter 11 case.

Finally, in some cases, a debtor's liquidation may be inevitable and beyond the control of any party.[220] Some companies that file for

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214. Of the 130 cases with a creditors' committee that result in either liquidation or reorganization, 128 cases include information about asset size, number of creditors, DIP financing, and secured claims. Controlling for these covariates, cases with at least one financial member are still significantly less likely to result in liquidation than are cases with no financial member ($p = .019$).

215. *See also supra* notes 5–24 and accompanying text (discussing the *FiberMark* case).

216. *See supra* Part IV.C.3.

217. *See infra* Appendix B.

218. Twenty cases involved prepackage or pre-arranged plans. Eight (40%) were NC, 4 (20%) were UCC, and 8 (40%) were OC.

219. *See supra* Part IV.C.4.

220. *See, e.g.*, Robert K. Rasmussen & David A. Skeel, *The Economic Analysis of Corporate Bankruptcy Law*, 3 AM. BANKR. INST. L. REV. 85, 89–90 (1995) (discussing the challenges in determining economic viability); Michelle J. White, *Does Chapter 11 Save Economically Inefficient Firms?*, 72 WASH. U. L.Q. 1319, 1319–21 (1994) (discussing corporate liquidation in Chapter 7 versus Chapter 11 and the challenges in determining economic viability).

Chapter 11 have outlived their economic utility and the process simply provides an organized means for distributing any remaining value to stakeholders.

B. Proposals for Mitigating Potential Undue Influence

As discussed above, the data are reason for thoughtful consideration. The data do not reflect certain information, and there is some truth to the proposition that every case is different. Nevertheless, strengthening the committee structure based on the information gleaned from the data will only improve the overall process.

Based on the data, Chapter 11 participants may benefit from an increased focus on committee composition, use of multiple committees, and increased public disclosures. The primary advantages of multiple committees are that they minimize potential conflicts and adverse perspectives within a single committee and enhance oversight of other parties in the process.[221] The primary disadvantage, of course, is the increase in administrative expenses incurred and paid by the debtor's estate.[222] The challenge then is to determine when, and to what extent, the potential advantages to multiple committees outweigh the cost disadvantage.

There probably is no one set of circumstances warranting multiple committee appointments—the determination should be made on a case-by-case basis. The size of the case, diversity among stakeholders, and level of stakeholder interest would be important factors. The bankruptcy courts and the U.S. trustee also could develop guidelines for multiple committee cases to maintain both procedural and cost control in those cases. For example, the guidelines could strongly encourage telephonic meetings and court appearances in appropriate circumstances; restrict the number of committee representatives who may participate in or appear at meetings and hearings; require the committees to divide investigatory duties, where appropriate, and share information on a confidential basis to minimize duplication; and perhaps cap the committees' professional fees, with

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221. As previously noted, the legislative history to section 1102 of the Bankruptcy Code suggests that Congress envisioned a multiple committee structure. *See, e.g.*, H.R. REP. NO. 95–595, at 235–36, *reprinted in* 1978 U.S.C.C.A.N. 5963, 6195 ("[T]he bill also provides for additional committees, with standing equal to that of the unsecured creditors' committee, when such additional committees are needed to represent various other interests in the case."); *supra* Part II.A.3.

222. *See, e.g.*, Gwynne, *supra* note 180, at 134 (discussing costs associated with multiple committees); Lubben, *supra* note 95 (analyzing factors leading to increased cost of bankruptcies).

the potential for increases if certain percentage recoveries are achieved for the committee's beneficiaries. A structured multiple-committee process may mitigate the downside to the formation and active participation of multiple committees.

In addition, in single-committee cases, the U.S. trustee should continue to focus on adequate representation of the general unsecured creditor body.[223] In making the adequate representation determination, however, creditors may benefit from a categorical representation approach. If a debtor's unsecured creditors include bondholders, suppliers, landlords, and employees, the creditors' committee should have one representative for each category of claims—that is, one bondholder or indenture trustee, one supplier, one landlord, and one employee. The U.S. trustee also could identify an alternate for each category so that, when a member resigns, a creditor from the same category can be easily identified and appointed to the committee.

This categorical approach is designed to mimic the effects of multiple committee cases on a smaller scale. A committee focused on equal representation among types of claims (and not concerned with claim amounts) likely would be more representative of the various perspectives held by the general unsecured creditor body than a committee comprising solely of the largest claimholders. A single committee also should impose lower administrative costs on the estate than the multiple committee structure. Nevertheless, it may be difficult to find creditors in each category who are willing to serve on

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223. Under the guidance of section 1102 of the Bankruptcy Code, the U.S. trustee generally selects committee members based on the amount of creditors' unsecured claims against the debtor. *See, e.g.*, 11 U.S.C. § 1102(b)(1) (2006) ("A committee of creditors appointed under subsection (a) of this section shall ordinarily consist of the persons, willing to serve, that hold the seven largest claims against the debtor of the kinds represented on such committee."). For example, consider the following Q&A provided by one of the offices of the U.S. trustee:

> Q: How are creditors appointed to the Official Committee of Unsecured Creditors?
>
> A: In most cases, the United States Trustee solicits the interest of the Twenty Largest Unsecured Creditors by mailing the creditors a Committee Acceptance Form. If there are sufficient responses to the solicitation, the United States Trustee will form an Official Committee of Unsecured Creditors. In selected cases, the United States Trustee conducts an Organizational Meeting where the presence of the creditor or the creditor's authorized representative (bearing a written authorization) is required. The United States Trustee forms a Committee by appointing creditors in attendance (in person or by proxy) at the Organizational Meeting.

Frequently Asked Questions, U.S. TRUSTEE PROGRAM, REGION 2, U.S. DEP'T OF JUSTICE, (Jan. 8, 2010), http://www.justice.gov/ust/r02/manhattan/faqs.htm#CH11Q2. If further study and consideration support a categorical approach to single committee composition, an amendment to the language of section 1102(b) likely will help facilitate a more uniform implementation of that approach.

the committee.[224] As discussed above, incentive to serve is an existing problem and may warrant further study.[225]

Creating representative committees that are effective in a Chapter 11 case requires not only the right parties but also additional information. The bankruptcy courts and the U.S. trustee can make informed decisions about the number and composition of committees only if they have all of the relevant information from the debtor and creditors. As such, debtors who do not file their schedules of assets and liabilities in a timely manner will need to submit at least basic information on the categories of their general unsecured claims and parties potentially holding those claims.[226] Moreover, creditors interested in serving on the committee need to make full disclosures regarding their claims against and interests in the debtor, its affiliates and insiders, and its competitors.

Notably, these types of basic disclosures should be required of any party actively participating in the Chapter 11 case—a sort of "say to play" rule. If a creditor or other party objects to the debtor's plan, submits a bid to purchase the debtor's assets, or otherwise seeks to be heard in the Chapter 11 case, the parties, including the bankruptcy court, need to know this information.[227] Although parties typically will say that they are creditors or hold a claim of a certain amount to establish standing under section 1109 of the Bankruptcy Code, they rarely provide the details of their full interest in the Chapter 11

224. The decision to serve on a committee typically is a cost-benefit analysis for a creditor. Accordingly, a small trade creditor may not find it efficient to serve, even if it is one of the few trade creditors available to represent that category of claims on the committee. Accordingly, after further study of the benefits to multiple committees or categorical single committees, it may prove advantageous and economically efficient to provide small economic incentives to creditors who serve on committees.

225. *See supra* note 101 and accompanying text (discussing challenges to active committee participation).

226. Rule 1007(a)(1) of the Federal Rules of Bankruptcy Procedure require debtors to file their schedules of assets and liabilities on the first day of the Chapter 11 case, with the bankruptcy petition. Many debtors do not follow this mandate, however, and often receive extensions of their deadline to file schedules pursuant to Rule 1007(a)(5). FED. R. BANKR. P. 1007(a).

227. As discussed *supra* note 185, disclosure issues for lawyers representing more than one creditor or shareholder often arise under Rule 2019 of the Federal Rules of Bankruptcy Procedure. An amendment to Rule 2019 is under consideration that would "expand the scope of its coverage and the content of its disclosure requirements." *Proposed Amendments to the Federal Rules Call for More Creditor Disclosure*, AM. BANKR. INST. J., Mar. 2010, at 10, 11 (setting forth language of proposed amendment). These amendments would not, however, apply to creditors or shareholders represented by separate lawyers, and certain of the suggested revisions (for example, the amount paid by the party for its claim or interest) may not be warranted.

case.[228] To the extent such disclosures might reveal confidential or allegedly proprietary information, the bankruptcy court is well suited to grant exceptions for cause or order other appropriate protections for the parties.

C. Policy Considerations in Mitigating Undue Influence

Chapter 11 is designed to pool a debtor's resources and level the playing field among creditors.[229] The automatic stay prevents individual creditors from dismantling the debtor piecemeal and provides the debtor an opportunity to catch its financial breath.[230] The process attempts to create an environment conducive to cooperation and value maximization. The committee structure should enhance this process.

Retooling the committee structure to embrace multiple committees when warranted and adopting a categorical approach to single committee composition would be a good first step. More balanced creditor representation will give a stronger voice to various creditor perspectives and mitigate the potential for undue influence by individual creditors. Requiring additional disclosures by parties participating on committees or in the case more generally will serve this same goal. More participation by better informed parties also aligns with the original purposes of section 1102 of the Bankruptcy Code.[231]

CONCLUSION

Congress envisioned an active and productive role for creditors' committees in Chapter 11 cases. Creditors' committees offer a potential solution to the collective action problem and a statutory monitor of the debtor's activities. The data suggest, however, that creditors' committees are not reaching their full potential and may be contributing to liquidations and lower creditor recoveries.[232]

Does the data support discarding the committee structure? Not necessarily. A more constructive approach is to use the data to

228. 11 U.S.C. § 1109(b) (2006) ("A party in interest, including the debtor, the trustee, a creditors' committee, an equity security holders' committee, a creditor, an equity security holder, or any indenture trustee, may raise and may appear and be heard on any issue in a case under this chapter.").

229. *See supra* Part II.A.

230. § 362 (describing the scope and content of bankruptcy automatic stay).

231. *See supra* Part II.A.3.

232. *See supra* Part IV.

strengthen the committee structure—going back to a role where committees "represent the various classes of creditors and equity security holders from which they are selected. . . . [and] protect their constituents' interests."[233] The proposed use of multiple committees, categorical single committees, and more robust disclosures targets that goal.[234] By striving to give more creditors a stronger, more informed voice on committees, the committee structure could help protect the process from the often subtle and questionable influence of just a few.

233. H.R. REP. NO. 95–595, at 235, *reprinted in* 1995 U.S.C.C.A.N. 5963, 6194.

234. *See supra* Part V.B.

APPENDIX A

Components of Database:

Step One:

For each jurisdiction, the authors ran a "Case Report" through PACER for each of the years implicated by the study. The Case Report listed only Chapter 11 cases filed in the jurisdiction during the applicable study period. Step One resulted in twenty-seven different Case Reports.

Step Two:

The authors then eliminated the following types of cases from each of the Case Reports:

- Individual cases
- Cases dismissed or converted within the first twelve months of the filing date
- Cases of affiliated or related debtors in jointly-administered cases

The following table shows the total number of cases in each Case Report following the review and elimination process of Step Two:

Year	SDNY	DE	NDIL	CDCA	MD	NDOH	Total
2002[235]	170	75	76				321
2003	147	61	47				255
2004	116	27	40	66	29	24	302
2005	109	27	39				175
2006	72	31	27				130
2007	62	36	34	62	33	21	248
2008	115	82	46				243
Total	791	339	309	128	62	45	1674
%	47.3	20.3	18.5	7.6	3.7	2.7	100.1[1]

[1]Total percentage does not sum to 100 due to rounding.

235. The case database includes one case filed in 2001. This case was the lead case in the Chapter 11 cases of the lead debtor and its affiliates. One of the affiliate debtors filed its case in 2002 and was selected for the database through the stratified random selection process. Consistent with the study's methodology, the lead case was substituted for the eliminated affiliate case. The authors considered replacing this case but elected to retain it for consistency purposes and because it was filed only five months before the study period.

Step Three:

The Bureau then randomly selected ten cases from each Case Report. This process yielded a total database of 270 cases.

Step Four:

The authors then used the LoPucki Business Bankruptcy Project database ("BBP") to identify all cases included in the BBP that were filed in a jurisdiction and year implicated by the study. This process yielded 146 cases, from which the Bureau randomly selected twenty-six cases that were not already included in the 270 cases identified in Step Three.

Step Five:

The authors and the Bureau selected a total of 296 cases for the database. The Bureau then assigned each case a token number and randomly allocated the cases among the four coders.

APPENDIX B

Specific Case Information[236]

Jurisdiction	**NC (n=144)**	**UCC (n=115)**	**OC (n=37)**	**Total**
District of Delaware				
Count	11	58	18	87
% within Jurisdiction	12.6	66.7	20.7	100.0
% within Committee Type	7.6	50.4	48.6	29.4
Northern District of Illinois				
Count	52	15	5	72
% within Jurisdiction	72.2	20.8	6.9	100.0
% within Committee Type	36.1	13.0	13.5	24.3
Southern District of New York				
Count	41	21	13	75
% within Jurisdiction	54.7	28.0	17.3	100.0
% within Committee Type	28.5	18.3	35.1	25.3
District of Maryland				
Count	13	7	—	20
% within Jurisdiction	65.0	35.0	—	100.0
% within Committee Type	9.0	6.1	—	6.8
Central District of California				
Count	14	5	1	20
% within Jurisdiction	70.0	25.0	5.0	100.0
% within Committee Type	9.7	4.3	2.7	6.8
Northern District of Ohio				
Count	12	8	—	20
% within Jurisdiction	60.0	40.0	—	100.0
% within Committee Type	8.3	7.0	—	6.8
Southern District of New York, but then transferred to another jurisdiction				
Count	1	1	—	2
% within Jurisdiction	50.0	50.0	—	100.0
% within Committee Type	0.7	0.9	—	0.7

236. Unless noted otherwise, all reported percentages reflect the percentage observed within a committee type.

Form of Business Entity[237]	**NC (n=144)**	**UCC (n=115)**	**OC (n=37)**	**Total**
Corporation	117 (82.4)	104 (90.4)	32 (88.9)	253 (85.3)
Partnership	2 (1.4)	1 (0.9)	1 (2.8)	4 (1.4)
Limited Partnership (or LLP)	2 (1.4)	1 (0.9)	— —	3 (1.0)
Limited Liability Company	21 (14.8)	9 (7.8)	3 (8.3)	33 (11.3)
Public Company	17 (11.8)	35 (30.4)	22 (59.5)	74 (25.0)
Small Business Debtor[238]	42 (29.2)	5 (4.3)	1 (2.7)	48 (16.2)
Single Asset Real Estate Debtor[239]	20 (13.9)	1 (0.9)	1 (2.7)	22 (7.4)
Debtor's Industry				
Agriculture, Forestry, and Fishing	1 (0.7)	1 (0.9)	—	2 (0.7)
Mining	1 (0.7)	—	1 (2.7)	2 (0.7)
Construction	6 (4.2)	3 (2.6)	1 (2.7)	10 (3.4)
Manufacturing	11 (7.6)	34 (29.6)	12 (32.4)	57 (19.3)
Transportation, Communications, Electric, Gas, and Sanitary Services	15 (10.4)	15 (13.0)	8 (21.6)	38 (12.8)
Wholesale or Retail Trade	13 (9.0)	27 (23.5)	2 5.4)	42 (14.2)
Finance, Insurance, and Real Estate	36 (25.0)	9 (7.8)	6 (16.2)	51 (17.2)
Services	60 (41.7)	20 (17.4)	6 (16.2)	86 (29.1)
Unknown	1 (0.7)	6 (5.2)	1 (2.7)	8 (2.7)

237. Some cases had unknown classifications. NC: 1.4% (n = 2), OC: 2.7% (n = 1).
238. Some cases had unknown classifications. NC: 2.1% (n = 3), UCC: 2.6% (n = 3).
239. Some cases had unknown classifications. NC: 2.8% (n = 4), UCC: 0.9% (n = 1).

Number of Affiliated Creditors	NC (n=144)	UCC (n=115)	OC (n=37)	Total
1–49	96 (66.7)	26 (22.6)	9 (24.3)	131 (44.3)
50–99	26 (18.1)	10 (8.7)	—	36 (12.2)
100–199	9 (6.3)	17 (14.8)	2 (5.4)	28 (9.5)
200–999	7 (4.9)	28 (24.3)	3 (8.1)	38 (12.8)
1,000 or more	2 (1.4)	33 (28.7)	33 (62.2)	58 (19.6)
Unknown	4 (2.8)	1 (0.9)	—	5 (1.7)
Total Assets (in dollars)				
Mean	37,216,000	57,676,000	7,305,000,000	903,250,000
Median	956,783	7,424,100	366,320,000	2,508,000
Total Liabilities (in dollars)				
Mean	47,858,000	107,560,000	1,552,500,000	248,910,000
Median	1,791,800	22,206,000	580,240,000	6,156,700
Gross Annual Income (last full preceding chapter 11 petition) (in dollars)				
Mean	24,500,000	115,970,000	1,013,700,000	177,170,000
Median	503,578	7,105,600	6,427,900	1,040,300

APPENDIX C

Table 1: Summary of Hierarchical Regression Analysis for Effect of Committee Type on Percentage Recovery (N = 162)

	Model 1			Model 2		
Variable	*B*	*SE B*	*Exp(B)*	*B*	*SE B*	*Exp(B)*
Constant	-1.12***	0.31	0.33	-1.69**	0.52	0.19
NC	1.04**	0.39	2.84	1.51**	0.51	4.54
OC	1.97***	0.50	7.17	1.82**	0.53	6.15
UCC (reference)						
Assets (≥ median)				1.14**	0.48	3.14
DIP Financing (approved)				-0.51	0.39	0.60
Nagelkerke R^2		.14			.20	

*p < .05. **p < .01. ***p < .001.

Table 2: Summary of Hierarchical Regression Analysis for Effect of Committee Type on Liquidation (N = 189)

	Model 1			Model 2		
Variable	*B*	*SE B*	*Exp(B)*	*B*	*SE B*	*Exp(B)*
Constant	0.52**	0.24	1.68	0.55	0.42	1.73
NC	-1.34***	0.34	0.26	-1.44***	0.41	0.24
OC	-2.20***	0.54	0.11	-2.37***	0.57	0.09
UCC (reference)						
Assets (≥ median)				0.88**	0.38	2.41
DIP Financing (approved)				-1.10**	0.39	0.36
Nagelkerke R^2		.19			.26	

*p < .05. **p < .01. ***p < .001.