
ARTICLE

THE CREDITORS' BARGAIN REVISITED

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Thirty-six years ago, Tom Jackson suggested that corporate bankruptcy law can best be explained and defended as the terms of an implicit bargain among creditors.¹ This assertion is founded on a belief that creditors, as a group, prefer bankruptcy's collective process to a grab race among themselves, particularly when such a race may cause the demise of a viable going concern.

Since Jackson's article, scholars have discussed and debated whether creditors need to rely on bankruptcy's bargain for collective action. Some have contended that creditors could in fact contractually arrange for a collective process and that the law should permit them to do so. Others have argued that the impediments to such a contractual arrangement would be too daunting. With rare exception, though, participants in this dialogue assumed that creditors desire some form of collective process, whether provided by statute or contract. That is, while implementation was debated, the collectivization premise went mostly unchallenged.

The recent transformation of the bankruptcy process from a forum of reorganization to, largely, an auction block further supports the collectivization premise. A collective process may not seem attractive when it

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¹ Thomas H. Jackson, *Bankruptcy, Non-Bankruptcy Entitlements, and the Creditors' Bargain*, 91 YALE L.J. 857, 859-71 (1982).

features the contests inherent in reorganization, described colorfully by Sol Stein as a feast for lawyers.² But the bankruptcy process may appear in a more favorable light when it is used simply to conduct an orderly sale of the debtor's assets, including a sale as a going concern if that configuration of assets garners the highest bid.

All may seem well, then, in the world of bankruptcy, where the apparent confluence of theory and practice led Douglas Baird and Robert Rasmussen to declare the end of bankruptcy,³ by which they meant that bankruptcy has evolved to its ideal. But there is a fly in the ointment.

At a series of recent conferences attended by academics and practitioners, the latter have suggested, sometimes expressly, that if freed from legal constraint, creditors they know would not only contract out of bankruptcy but out of any collective proceeding. That is, at least some practicing lawyers—presumably not immersed in Jacksonian orthodoxy—seem to believe that their clients would like to engage in a grab race after all, consequences be damned.

Do these lawyers, who represent sophisticated lenders, simply mean that their clients favor a competition in which they would occupy a privileged position? Perhaps. But this seems unlikely because in a functioning capital market, creditors are mere stakeholders who are forced by the market to pay for any privilege in the form of lower interest rates. Sophisticated lenders, along with their lawyers, well understand this.

But perhaps a better explanation for why lenders might forgo collectivization exists: debtors would insist on interest rates possible only if the debtor obtained funds within a capital structure designed to throw the firm to the creditor wolves in the event of an uncured default. This conjecture is not new. I first raised the idea years ago in dissent to the collectivist hegemony. What is new, and the focus of this Article, is the extent to which the conjecture is supported by recent developments in bankruptcy practice and creditor activism.

I. THE CREDITORS' IMPLICIT BARGAIN

On the desirability of collective action, almost all were Jacksonians once, myself included. In an article I wrote some years ago,⁴ I invoked Thomas Jackson to explain that, at its core, bankruptcy serves creditors as a group when it supplants individual creditor debt collection remedies with a

² See SOL STEIN, *BANKRUPTCY: A FEAST FOR LAWYERS* 303 (1999) (“[Chapter 11] is a refuge for a few opportunists and a feast for many lawyers. For the leaders of businesses trapped in it, Chapter 11 is the twentieth-century equivalent of the eighteenth-century pillory, a dehumanizing, inefficient public spectacle.”).

³ Douglas G. Baird & Robert K. Rasmussen, *The End of Bankruptcy*, 55 STAN. L. REV. 751 (2002).

⁴ Barry E. Adler, *A World Without Debt*, 72 WASH. U. L.Q. 811, 812-13 (1994).

“collective debt-collection device.”⁵ In theory, as I said then, bankruptcy’s collectivized proceeding is superior to individual creditor actions because individual creditors have perverse incentives to act in their own interests, even if those interests disserve the creditors’ collective interest. Thus, I joined the consensus that bankruptcy is beneficial to the extent it protects creditors from their own worst instincts.

To elaborate slightly, assume a debtor firm operates a business worth more as a going concern than if its assets were sold piecemeal. That is, the assets are worth more as parts of the debtor’s business than they are distributed separately to become parts of other businesses. Assume further that the debtor is subject to obligations even greater than the value of the firm as a going concern and that the debtor is in default on those obligations. The debtor has insufficient assets to pay all creditors in full, so each creditor may have an incentive to collect on its debt before the debtor’s assets are depleted by other creditors’ collections. In the absence of bankruptcy law, a creditors’ race to the assets could divide those assets piecemeal, with each race winner taking a piece of the debtor large enough to satisfy its own claim. As a result, the creditors could take from the debtor assets worth in the aggregate only the piecemeal liquidation value.

Foundational to the Jacksonian creditors’ bargain paradigm is that, without bankruptcy law, a potentially destructive creditor grab race would be inevitable. The premise is that such a race—rather than an actual bargain among creditors—would occur because each creditor would know that it could be left without recourse to any assets if it delayed its own action on the mere hope that the creditors would both find one another and agree to act collectively. This presumed dilemma of coordination presents a collective action problem.

Bankruptcy solves a creditors’ collective action problem by disallowing individual creditor action. A bankruptcy court supervises the use and disposition of the debtor’s assets and can hold the assets together to maximize their value. The court then divides the value of the assets among creditors in an orderly fashion, either through the sale of the assets to a third party and the distribution of sale proceeds or through the distribution of interests in a debtor freed from prebankruptcy obligations. In no instance does an individual creditor have an opportunity to withdraw vital assets unilaterally.

In the illustration above, for example, the bankruptcy court would prohibit individual creditor action and could sell the debtor’s business as a going concern or distribute securities in the firm with an aggregate worth equal to the value of the firm as a going concern. This sale or distribution would thus preserve the debtor’s going-concern surplus. Such bankruptcy intervention is thought to reflect a hypothetical creditors’ bargain or the

⁵ THOMAS H. JACKSON, *THE LOGIC AND LIMITS OF BANKRUPTCY LAW* 7 (1986).

solution the creditors would reach could they solve their coordination problems. Accordingly, bankruptcy's solution to the collective action problem is the chief justification for its elimination of individual creditor remedies.

Douglas Baird has summarized this analysis as follows: "[W]e may not desire a world without bankruptcy because the self-interest of creditors leads to a collective action problem, and a legal mechanism is needed to ensure that the self-interest of individuals does not run counter to the interests of the group."⁶

II. A CREDITORS' EXPRESS BARGAIN

Against this background, a number of scholars considered the possibility that creditors desirous of collective action need not rely on an implicit bargain. Rather, they might enter an actual bargain that deprived individual creditors of unilateral collection rights. Robert Rasmussen, for example, suggested that bankruptcy law could be adopted, or forgone, by a corporate debtor based on a selection from options in a federal register that he proposed.⁷ David Skeel suggested allowing states to draft their own insolvency laws applicable to companies incorporated under the laws of that state.⁸ My own proposal was that debtors could, possibly even under extant law, adopt a charter provision that foreswore the issuance of traditional debt, which would be replaced by investment instruments that I called Chameleon Equity. Such instruments would allow a firm to retain the benefits of debt's fixed obligations with automatic—in today's jargon "self-executing"—conversion to debt on uncured default.⁹

Whether ruled by a menu selection in a federal register, a debtor's choice of state corporate law, or a charter provision applicable under the laws of any state, a creditor who loaned to a debtor subject to a particular set of insolvency rules could be deemed to have chosen a bargain reflected in those rules.¹⁰ And

⁶ Douglas G. Baird, *A World Without Bankruptcy*, 50 LAW & CONTEMP. PROBS., Spring 1987, at 184.

⁷ See Robert K. Rasmussen, *Debtor's Choice: A Menu Approach to Corporate Bankruptcy*, 71 TEX. L. REV. 51, 100 (1992) ("[A] menu of bankruptcy-law selections . . . allows those in the best position to make the decision to select which bankruptcy term maximizes their expected value.").

⁸ See David A. Skeel, Jr., *Rethinking the Line Between Corporate Law and Corporate Bankruptcy*, 72 TEX. L. REV. 471, 513 (1994) (arguing that state regulation of corporate bankruptcy is the "most promising response to the inefficiencies of the current regime").

⁹ See Barry E. Adler, *Financial and Political Theories of American Corporate Bankruptcy*, 45 STAN. L. REV. 311, 324 (1993) [hereinafter Adler, *Financial and Political Theories*] (explaining that a Chameleon Equity holder "would possess the same right as a creditor to set payments from the firm, but it would not be permitted to collect individually on an obligation in default"). That article elaborated on a suggestion published earlier. See generally Barry E. Adler, *Bankruptcy and Risk Allocation*, 77 CORNELL L. REV. 439 (1992) [hereinafter Adler, *Risk Allocation*].

¹⁰ To be sure, nonconsensual creditors do not make voluntary loans and cannot be said to have chosen any insolvency regime. For this reason, as I have argued elsewhere, tort creditors should have highest priority in any insolvency regime. See Adler, *Financial and Political Theories*, *supra* note 9, at

while one might say that only the charter provision, which would restrict investment contracts to terms required by those provisions, could properly be labeled an actual bargain among creditors, with choice of law by the debtor imposed on creditors without actual assent, this would be a mere quibble. By contrast to a single federal bankruptcy rule that overrides any state law or charter provision, any method through which creditors can choose to extend credit under one set of rules or another can, for most purposes, be considered an actual bargain.¹¹

As I have observed previously in fleshing out how a contractual alternative to bankruptcy might look, it is useful to distinguish bankruptcy policy, by which I mean collective action policy, from issues of general concern. A tenet of the Jacksonian paradigm is that legal provisions directed to the latter need not be part of an insolvency regime. It follows that if there is no need for a legal mechanism to prevent a creditors' grab race, there is no need for any sort of special insolvency regime. The contractual collective-action mechanism that I proposed, born of a thought experiment about a world without debt, suggests that there is no need for any legal mechanism beyond contract enforcement to ensure collective action, and thus, no need for corporate bankruptcy law or any special insolvency regime.

Of course, the simplest contractual alternative to bankruptcy as an insolvency process is for firms to issue only common equity, which eliminates the possibility of insolvency, or to issue debt only to a single creditor, which eliminates any collective action problem among creditors. But it had long been believed that such a response to the risks of insolvency would be unworkable. A firm might rationally issue fixed obligations, even ignoring any potential tax benefits, because such obligations for some firms can allow managers to hold a significant portion of a firm's residual claim and can for all firms subject managers to the consequences of payment default, including, perhaps, dismissal. The result could be more productive managers. A firm might rationally issue its fixed obligations to a large number of investors if no single lender would be willing to provide all financing at all times—as might be the case, or has been the case, for some large issuers. Or a firm might rationally prefer to have multiple financing sources so as not to vest in any lender the opportunity to behave strategically with respect to subsequent loans that only an existing lender, given better information, could efficiently provide.

With the assumption in mind that large firms would issue a significant amount of fixed obligations to multiple creditors, I imagined

340 (“Ideally, nonconsensual claimants would have highest priority in any sort of firm.”). This point, however, is beyond the scope of this Article.

¹¹ For an analysis of any such bargain's financial consequences, see generally Alan Schwartz, *Bankruptcy Workouts and Debt Contracts*, 36 J.L. & ECON. 595 (1993).

eliminating only a single feature of traditional debt: the right of an individual fixed-obligation claimant to collect. This one feature is significant because it is the feature of debt that creates the collective action problem and the need for bankruptcy reorganization law.

Firms that issue fixed obligations to multiple investors might benefit from a debt-free capital structure by avoiding the expense of financial restructuring, either through bankruptcy or other means. This expense can be significant when claimant negotiations deteriorate into an imbroglio, as they frequently did at the time that I first engaged in this thought experiment during the 1990s.¹² Taking as given the desire to protect insolvent but viable firms, it is not clear that anything significant would be lost by eliminating collection rights.

Elimination of debt, and with it the individual creditor's right to collect, might cost little because there is an alternative collective remedy of which fixed-obligation claimants could avail themselves. I argued that a firm could, in principle, replace debt with a special variant of preferred equity. The Chameleon Equity firm that would result would retain the benefits of fixed obligations but would avoid the negative consequences of creditor coordination failure—notably postdefault dismemberment of a viable firm. In the simplest Chameleon Equity firm, if insolvency—defined as asset value less than fixed obligations—led to default, default would eliminate the preinsolvency common-equity class and would convert the lowest priority fixed-obligation class to common equity. Any remaining senior class would survive unaffected. At any given time, management would represent the firm's current common-equity class.

Significantly, even in a complex firm, one with a variety of fixed-obligation priorities, no court would have to preserve the higher obligations' priority. The senior obligations would retain their priority because they would survive complete with fixed claims. This would free the firm to adopt a tiered hierarchy of priority classes that would keep the firm almost eternally solvent and almost eternally subject to significant fixed obligations. In the end, every claimant would get the priority for which it contracted. And although there would be questions of default and liability, as there are now in traditional firms, there would be no

¹² For an estimate from that time of bankruptcy reorganization's direct costs, see Lawrence A. Weiss, *Bankruptcy Resolution: Direct Costs and Violation of Priority of Claims*, 27 J. FIN. ECON. 285, 288-90 (1990), in which the author examines the direct costs of bankruptcy, including the legal, professional, and administrative fees associated with bankruptcy filing. There are, moreover, indirect costs that will not be reflected in ex post measurements of financial distress costs. That is, there are costs from the tendency of expensive bankruptcy proceedings to reallocate a firm's value from high- to low-priority claims, thus reducing the value of high-priority claims to firms that wish to issue such claims. See, e.g., Adler, *Risk Allocation*, *supra* note 9, at 440; Alan Schwartz, *The Absolute Priority Rule and the Firm's Investment Policy*, 72 WASH. U. L.Q. 1213, 1214 (1994) (arguing that a relaxed absolute priority rule "worsens investment incentives").

postinsolvency restructuring expense even where the auction of the debtor as a going concern were not a viable option. A Chameleon Equity firm would have to bear the initial transaction costs of adopting the Chameleon Equity structure. But it is difficult to imagine that these costs would be, in the long run, anything but trivial additions to the current costs of contracting for corporate charters and bond covenants. In short, corporate bankruptcy would appear to be unjustified.

Even then, I was not so naive as to believe that abolition of bankruptcy or firm selection of a Chameleon Equity structure was imminent or even possible. In my original paper on Chameleon Equity, I described a list of legal and other impediments to a Chameleon Equity structure.¹³ These include tax, commercial, corporate, and tort law.¹⁴ I also offered a public choice explanation for the persistence of these impediments.¹⁵ Nevertheless, in principle, a world without debt or bankruptcy and with contractual solutions to the collective action problem seemed an efficient world.

III. THE REAL WORLD

These proposals for contractual alternatives to bankruptcy were perhaps intriguing, and they certainly produced some interesting debates before the turn of the new millennium.¹⁶ But these academic debates did not, then or since, influence policy. Moreover, it was not only legislators who failed to take up the call. To my chagrin, despite dizzying financial innovation, debtors and investors did not attempt the firm-wide Chameleon Equity structure I proposed.¹⁷ To be sure, as noted above, I had identified legal impediments to

¹³ Adler, *Financial and Political Theories*, *supra* note 9, at 333-41.

¹⁴ *Id.*

¹⁵ *Id.* at 341-46.

¹⁶ A sampling of these debates emerged from Washington University School of Law's Interdisciplinary Conference on Bankruptcy and Insolvency Theory. See Adler, *supra* note 4; James W. Bowers, *Rehabilitation, Redistribution or Dissipation: The Evidence for Choosing Among Bankruptcy Hypotheses*, 72 WASH. U. L.Q. 955, 956-57 (1994) (describing the misgivings of the academic community regarding bankruptcy's efficiency in the late 1980s and early 1990s); Samuel L. Bufford, *What Is Right About Bankruptcy Law and Wrong About Its Critics*, 72 WASH. U. L.Q. 829, 839 (1994) (questioning the usefulness of Chameleon Equity in the vast majority of bankruptcy cases); Karen Gross, *Taking Community Interests into Account in Bankruptcy: An Essay*, 72 WASH. U. L.Q. 1031, 1037-38 (1994) (noting that conference proposals for alternatives to the bankruptcy system fail to address problems on the human level); Robert K. Rasmussen, *The Ex Ante Effects of Bankruptcy Reform on Investment Incentives*, 72 WASH. U. L.Q. 1159, 1193 (1994) ("Despite [some] gains, the move to an automatic cancellation system [like Chameleon Equity] would not be unambiguously beneficial."); Elizabeth Warren & Jay Lawrence Westbrook, *Searching for Reorganization Realities*, 72 WASH. U. L.Q. 1257, 1261 (1994) (discussing how both Chameleon Equity and a menu-based bankruptcy alternative would require "a major reform of tort law, of the law governing obligations owed to government entities, and of laws governing other obligations to involuntary creditors").

¹⁷ Bail-in bonds issued in Europe after the 2008 financial crisis look much like the Chameleon Equity obligations I proposed, but these bail-in bonds, referred to in recent literature also as contingent convertible, or CoCo, bonds, replace only the most junior levels of debt.

Chameleon Equity, but I became unconvinced that these impediments were so formidable as to prevent even attempts at the proposed capital structure if that structure were as valuable as I had claimed it might be.

Perhaps, then, Chameleon Equity or any other contractual alternative to corporate bankruptcy is theoretically sound but offers only insignificant advantages over even an imperfect, but largely functioning, bankruptcy regime such as that of the United States. It could be, therefore, that a contractual alternative to resolve the collective action problem would be more important elsewhere—in transitional economies, for instance.¹⁸

There is, however, a potentially more fundamental explanation for why firms have not attempted to innovate toward a pure Chameleon Equity firm. The potential explanation is that threat of liquidation in an asset-grab race by dispersed holders of traditional debt may be a *solution* rather than a problem.

As I have previously observed,¹⁹ there are, theoretically, two approaches to corporate insolvency. A system structured according to an *ex post* approach relies on a court-supervised examination of a firm that cannot pay its debts in full. If this examination reveals the firm to be viable despite its financial distress, the firm restructures its liabilities, or is auctioned as a going concern, and continues. Otherwise the firm ceases operation and is liquidated piecemeal. Corporate bankruptcy laws in the United States and in other countries adopt this approach. Under an alternative, *ex ante* approach, investors would instead abide by the consequences of predictions made at the time of investment about a firm's likely value and attributes should it become unable to pay its debts. Unless initial investment contracts provided otherwise, a firm's failure to satisfy its obligations would subject its assets to collection without any after-the-fact attempt to determine whether the firm were economically viable. Viable firms could be liquidated in the process. But such an *ex ante* approach may be optimal, despite any contrary intuition.²⁰

A misapprehension of financial economics gives rise to the intuition that a proper insolvency system must screen firms that should live from those that should die. It is an axiom of finance theory that a firm's financial health—its ability to pay its debts—is not synonymous with the firm's economic health—its ability to provide goods or services efficiently. Thus, if insolvency provided no clue as to a firm's viability, legal rules that permitted a firm's immediate dismemberment at the hands of unconstrained creditors might waste much value. But a firm's insolvency, as signaled by the firm's

¹⁸ In a separate paper, I have argued just that. See Barry E. Adler, Bernard Petrie Professor of Law & Bus., N.Y. Univ., Keynote Address at the Tsinghua University Law School Sixteenth International Twenty-First Century Commercial Law Forum: Contractual Corporate-Insolvency Resolution in Transitional Economies (Oct. 2016) (on file with author).

¹⁹ See Barry E. Adler, *A Theory of Corporate Insolvency*, 72 N.Y.U. L. REV. 343, 343-44 (1997).

²⁰ *Id.*

default on its debt, may provide a strong clue as to the firm's viability. Financial distress need not randomly befall good and bad firms alike. Because investors choose an initial capital structure, they may adopt a debt component that renders unlikely the simultaneous occurrence of insolvency and viability. Consequently, investors might well prefer insolvency rules that channel few resources into distinguishing firms that should continue from those that should liquidate, even if the result is routine liquidation.

So perhaps the reason firms do not innovate toward a contractual collective insolvency proceeding is that the innovation they'd really like is *abjuration* of a collective proceeding. This is an attractive hypothesis in part because there are numerous examples of debtors that attempt to exempt individual creditors from the bankruptcy process—borrowing through Special Purpose Entities, for example.²¹ And although we don't see firms attempting to opt out of bankruptcy entirely, this may well be because it is, or has been, commonly believed that such an opt-out would not be honored under current bankruptcy law, an avowed purpose of which is to refinance viable but insolvent debtors. That is, while there may be only weak legal barriers to a Chameleon Equity structure, which facilitates debtor rescue, there may be an impenetrable barrier or an advanced disavowal of such rescue.

Although this analysis does represent a challenge to the creditors' bargain hypothesis, I have not before described it as such primarily because these conclusions rest on what I myself describe as an untestable hypothesis. Debtors do not attempt a wholesale opt-out of bankruptcy's collective proceeding. Jacksonians (and perhaps Jackson himself) attribute this to debtor satisfaction with collectivization. I attribute the same behavior to apathy

²¹ In his thoughtful comments at this conference, Ted Janger questioned the relevance of my observation that some debtors attempt to exempt some creditors from bankruptcy's collective process. He took a Rawlsian approach to the matter and suggested that while creditors behind a veil of ignorance would opt in to collectivization, those whom we see opting out know their place in the pecking order and perceive an advantage in doing so. This is an interesting observation but also largely inapposite. It is important to keep in mind that the creditors' bargain is, like the Rawlsian veil, only a metaphor. If bankruptcy reflects the creditors' bargain, then it also reflects the debtors' interests. As noted in the introduction to this Article, in a competitive capital market, creditors are mere stakeholders for debtor interests. Truly relevant, then, is the credit-collection regime the *debtors* choose. Consequently, if a debtor attempts to exempt a particular creditor from the bankruptcy process, it is the debtor's choice, not the creditor's, and such an attempt at exemption is an indication that the debtor does not believe collectivization minimizes its cost of capital. This is so, at least, if the attempted exemption precedes the issuance of other debt, as may be the situation in at least some debtor adoptions of special interest vehicles, for example. In any case, the speculation made here is that debtors would, if given the choice, opt out of collectivization from the start, before any credit is issued, and while all creditors, prospectively, might be said to be behind the veil of ignorance. This is, moreover, how I understand the practitioners' conjecture on their clients' desire to opt out of bankruptcy, a conjecture described in the introduction.

given the perceived futility of action. This is a thin reed—and, as explained above, one I've relied on before, to my regret. That said, given recent events, and for reasons I'll next address, I've now grown (slightly) bolder.

IV. THE END OF BANKRUPTCY

In the opening paragraph of a widely read and highly regarded article, Douglas Baird and Robert Rasmussen describe a sea change in bankruptcy reorganization as that process had been practiced and understood:

Corporate reorganizations have all but disappeared. Giant corporations make headlines when they file for Chapter 11, but they are no longer using it to rescue a firm from imminent failure. Many use Chapter 11 merely to sell their assets and divide up the proceeds. TWA filed only to consummate the sale of its planes and landing gates to American Airlines. Enron's principal assets, including its trading operation and its most valuable pipelines, were sold within a few months of its bankruptcy petition. Within weeks of filing for Chapter 11, Budget sold most of its assets to the parent company of Avis. Similarly, Polaroid entered Chapter 11 and sold most of its assets to the private equity group at BankOne. Even when a large firm uses Chapter 11 as something other than a convenient auction block, its principal lenders are usually already in control and Chapter 11 merely puts in place a preexisting deal. Rarely is Chapter 11 a forum where the various stakeholders in a publicly held firm negotiate among each other over the firm's destiny.²²

That article, although written not long after those described in the prior sections of this Article, describes a marked transformation in bankruptcy reorganization as that process had been practiced and as it had been understood at the time of those earlier writings.

At the risk of oversimplification, what Baird and Rasmussen describe is a shift away from a potentially expensive imbroglio over valuation and entitlement to a rapid disposition. This disposition may take the form of either a free-and-clear sale of the assets to the highest bidder followed by a distribution of proceeds down the priority waterfall or, simpler still, a turnover of the assets to a united group of lenders whose priority claims would go unsatisfied, despite taking all, leaving no valid complaint for downstream creditors. One might say, then, that what Baird and Rasmussen describe is not so much the end of bankruptcy, but its evolution toward its ideal.

That bankruptcy has evolved, and is not truly at an end, is significant for the purposes of this Article because the changes that Baird and Rasmussen describe do not include an elimination of a collective proceeding. In the new

²² Baird & Rasmussen, *supra* note 3, at 751-52 (footnotes omitted).

world of corporate bankruptcy, there is perhaps little traditional reorganization, but assets are held together away from individual creditor collection until the court can decide what to do with them. The assets may eventually be sold in piecemeal liquidation, as in the examples given by Baird and Rasmussen, but they may instead be sold as a going concern if that brings the best price. Alternatively, assets are held together until the court can determine that the firm belongs to and can be run, or disposed of, by what Baird and Rasmussen describe as the “principal creditors.”

This is not to say that the changes in corporate bankruptcy are irrelevant for the question of whether a collective proceeding is desirable; far from it. Rather these changes increase the plausibility that collectivization does not, in fact, reflect the creditors’ implicit bargain.

The anecdotal list of liquidations in the Baird and Rasmussen article is supported by more formal analysis: in the new world of corporate bankruptcy, it is now common even for publicly traded firms to disappear rather than continue, in any form or under any ownership, as going concerns.²³ So in the years since I first speculated in the Chameleon Equity article that corporate bankruptcy is unnecessary for a firm with a capital structure designed to accommodate insolvency and default, it seems that just such structures have arisen, though not in the way I originally imagined. The high liquidation rate *in* bankruptcy, just mentioned, is testament to the fact that by the time bankruptcy is available to rescue debtors from the wolves, there may well be nothing to rescue. For such firms, the imposition of bankruptcy’s stay on individual creditor action may do little more than interfere with and delay the redeployment of assets, which creditors could otherwise quickly claim and sell.

To be sure, not all debtors that enter bankruptcy are worth more dead than alive. As noted above, the liquidation of viable debtors, if few enough, could be a price worth paying if freedom from bankruptcy’s collective process permitted the unhindered liquidation of the rest. But even that price would not be as high as may first appear. For the viable debtors, it is important to consider the role of “principal creditors.” It is now common, more common even than when Baird and Rasmussen wrote, for debtors to enter bankruptcy entirely pledged to a senior secured creditor—or a consortium of or trustee for such creditors—who will under no circumstances be repaid in full. Under principles of absolute priority, such creditors are entitled to the entire firm and have an incentive to keep its business afloat should the firm remain economically viable despite even a dire financial situation. Presumably, these principal creditors—the dominance of which in large part prompted a

²³ See, e.g., Barry E. Adler, Vedran Capkun & Larry Weiss, *Value Destruction in the New Era of Chapter 11*, 29 J.L. ECON. & ORG. 461, 464 (2013) (referring to a collection of empirical studies that support anecdotal accounts of a shift toward creditor control and liquidation in bankruptcy proceedings).

significant reform effort by the American Bankruptcy Institute²⁴—could be expected to assert their property interest ahead of other creditors even without bankruptcy intervention,²⁵ which may impede more than protect.

While Baird and Rasmussen may have been premature in declaring the end of corporate bankruptcy, perhaps their title was aspirational, or, at least, one can argue that it should have been if the purpose of bankruptcy is to prevent a creditor race to assets.

V. CONCLUSION AND THOUGHTS ON ASSET LAUNDERING

As noted at the start of this Article, these remarks were prompted by conversations at conferences such as the one for which the Article was written. In these conversations among academics and practicing lawyers, sophisticated practitioners gave the impression or stated outright that investors would, if they could, forswear the bankruptcy process. And my hope is that what I've written here will provoke a more focused consideration of that prospect.

Before concluding, though, I want to add another topic to the mix—an idea also prompted by conversation among academics and practitioners. Although there may be an implicit consensus that lenders are not particularly interested in forced collectivization, there is apparently a strong interest in another aspect of the bankruptcy process: free-and-clear dispositions. Without the cleansing available by a sale of assets through bankruptcy, or a discharge upon Chapter 11 plan confirmation, purchasers or creditors are at risk that state law actions will follow assets into the hands of a solvent entity.²⁶ This prospect would be unwelcome as well as unwise if the disposition of assets from an insolvent debtor failed to cure the insolvency problem, requiring another disposition, and so on. And the prospect would be unwelcome to some creditors, though not necessarily unwise, if it effectively elevated the priority of these asset-following

²⁴ See AM. BANKR. INST., AMERICAN BANKRUPTCY INSTITUTE COMMISSION TO STUDY THE REFORM OF CHAPTER 11 OF THE U.S. BANKRUPTCY CODE: REPORT AND RECOMMENDATIONS 214-24 (2014) (“Throughout their deliberations, the Commissioners held lengthy and thoughtful discussions concerning the rights of senior creditors in bankruptcy and how best to balance these rights with the reorganization needs of the debtor and the interests of other stakeholders.”).

²⁵ It is sometimes claimed that the bankruptcy process is necessary for a secured creditor to enforce a blanket lien on all assets, including the debtor's going-concern value. One might wonder whether a creditor who claims a blanket lien in bankruptcy should prevail if the claimed interest is unenforceable under state law. Even if a blanket lien is both legitimate and unenforceable under state law, it is not the classic Jacksonian collectivity function that is served when bankruptcy enforces such a lien in competition with junior creditors who, as a result of the lien, lack any claim to the debtor's assets. Put another way, adjudication of the winner in a grab race is not the same function as elimination of that race. And although an adjudication of a lien's validity prior to bankruptcy or state foreclosure proceedings entails a temporary suspension of asset distribution, such interference with creditor collection could be minimal.

²⁶ See *supra* note 25.

claims, which may be nonconsensual and thus entitled under nonbankruptcy law to no special priority.²⁷

So corporate bankruptcy may be desirable after all, even today. But bankruptcy's principal function may be asset laundering, not collectivization, the brilliant Jacksonian paradigm notwithstanding.

²⁷ See *supra* note 10.

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