DEFINING SUCCESS IN BUSINESS BANKRUPTCIES*

by Kenneth N. Klee**

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"There is no algorithm for a just society. Chaos in law describes human life."


**Introduction**

A debate is raging in bankruptcy circles over the desirability of chapter 11 of the Bankruptcy Code. Opponents of chapter 11 assert that it is a failure and should be repealed. Supporters counter that chapter 11 is a success and should be retained or at most fine tuned. But neither side of this debate has defined the concept of success. As a result, the debate lacks focus. To sharpen the pending debate, this article addresses the concept of success in the context of business bankruptcies.

As a matter of policy, we should define success to optimize social enterprise value rather than the direct, quantifiable, economic value for monied interests in a particular case. Determining optimal social value requires us to evaluate soft variables that are unquantifiable or not easily quantified. We should also consider the interests of employees, communities, and others who do not have a direct right to payment against the debtor. While we should use statistical analysis of quantifiable data to aid our evaluation of success, we must be careful to avoid ignoring or dwarfing soft variables or indirect interests that may be important elements of success. We can use chaos theory and pattern recognition to help us approach the problem of defining success in business bankruptcies. Ultimately, we should reform the law to improve the performance of the business bankruptcy system in achieving success.
In order to provide a framework to discuss the concept of success in a bankruptcy context, Part I provides a brief history of business bankruptcy law in the United States. This part discusses the roots of bankruptcy law in the United States and some of the implications that will shape our definition of success. The chapter 7 liquidation case is briefly differentiated from the chapter 11 business reorganization case.

Part II explores various models or philosophies of success outside the bankruptcy context. The concept of success is not monolithic, and it is necessary for us to select a concept of success that we can apply in the business bankruptcy context. This part examines lay and philosophical understandings of success. Part II also discusses economic models of success and concludes by introducing chaos theory as a model to define success.

Part III defines success for chapter 7 business liquidation cases. This part develops the basics of the chapter 7 business liquidation process and alternatives to chapter 7. This article identifies competing and conflicting goals of monied and governmental interests that are involved in chapter 7. After discussing the relative differences of particular perceptions of success, Part III adopts a definition of success from a broader perspective of maximizing value to society. The article contends that success of the chapter 7 business liquidation system depends in part on whether it is just, speedy, and inexpensive. Using this broader definition of success, the article proceeds to apply traditional statistical measures of success to evaluate the success of business liquidation cases. Part III concludes by noting that although we could use measures of success beyond traditional statistical measures to evaluate success of the
chapter 7 business liquidation system, those measures are probably approximated by traditional economic measures, due to an absence of fairness issues in the chapter 7 context.

Part IV builds on the relatively simple chapter 7 model of success. This part begins by describing the basics of the chapter 11 process and identifying some of the complexities and uncertainties that are inherent in chapter 11, such as the constituents' indeterminance about the future viability of the business and its value. Part IV next considers the competing and conflicting goals of the various constituencies in the chapter 11 process. This part concludes by measuring and defining success in chapter 11 business reorganizations. The analysis moves beyond traditional economic measurements to consider other more appropriate measures of success and develops the concepts of social enterprise value and social liquidation value. The Appendix defines these concepts more fully and considers balancing quantifiable and unquantifiable components.

Part V suggests some of the ways Congress might make business bankruptcy law more successful. The article encourages Congress to consider excluding certain kinds of cases, where the cost to society is likely to be far greater than the benefit from allowing these cases to proceed.
I. A Brief History Of Business Bankruptcy In The United States.

This part briefly examines the history of American bankruptcy law and its implications for our definition of success of the business bankruptcy system.

A. The Roots Of American Business Bankruptcy Law.

The grouping together of business liquidation cases and business reorganization cases is largely an historical accident.\footnote{At the time of the constitutional debates, bankruptcy in England was used to divide the assets of merchants. See CHARLES WARREN, BANKRUPTCY IN UNITED STATES HISTORY 5-6 (1935). The legal construct of business reorganization had not been developed. Thus it is not surprising that the Framers failed to provide for it expressly. Although rudimentary provisions for arrangements were included in section 43 of the Bankruptcy Act of 1867, reorganization provisions did not develop until the last thirty years of the 1800s, when the financial problems of the nation’s railroads required judicial intervention. VERN COUNTRYMAN, CASES AND MATERIALS ON DEBTOR AND CREDITOR 236 n.2 (2d ed. 1974). Initially, railroads were reorganized in equity receiverships. See, e.g., Northern Pac. Ry. v. Boyd, 228 U.S. 482, 33 S. Ct. 554 (1913); In re Reisenberg, 208 U.S. 90, 28 S. Ct. 219 (1908) (invoking receivership of New York City Ry. and Metropolitan Ry.); Louisville Trust Co. v. Louisville, N. A. & C. Ry., 174 U.S. 674, 19 S. Ct. 827 (1899); Foster v. Mansfield, C. & L.M. R.R., 146 U.S. 88, 13 S. Ct. 28 (1892); Alden v. Boston, H. & E. R.R., 1 Fed. Cas. 323 (S.D.N.Y. 1871)(No. 152). But it quickly became apparent that a statute was needed to embody rules of reorganization. The Railroad Reorganization Act of 1933, ch. 204, 47 Stat. 1467, 1474, enacting § 77 of the Bankruptcy Act, was such a statute. Ultimately, this form of relief was extended to almost all corporations with the enactment of § 77B of the Bankruptcy Act in 1934. Act of June 7, 1934, ch. 424, 48 Stat. 911, 912. Congressional efforts to expand the bankruptcy power to cover railroad reorganizations and corporate reorganizations were challenged almost immediately. When it became necessary to determine the legitimacy of the legal system of railroad reorganization under § 77, the Supreme Court validated the effort under the Bankruptcy Clause of the Constitution. Continental Ill. Nat'l Bank & Trust Co. v. Chicago, R.I. & P. Ry., 294 U.S. 648, 55 S. Ct. 595 (1935). The Courts of Appeals also upheld the constitutionality of business reorganizations under § 77B. E.g., Grand Boulevard Inv. Co. v. Strauss, 78 F.2d 180, 182-85 (8th Cir. 1935); Campbell v. Allegheny Corp., 75 F.2d 947, 951-55 (4th Cir.), cert. denied, 296 U.S. 581 (1935); Union Trust Co. v. Wagner (In re Central Funding Corp.), 75 F.2d 256, 260-61 (2d Cir. 1935).}

Traditionally, bankruptcy has served as a collective proceeding to divide the proceeds of the assets of a failed business for the purpose of repaying creditors.\footnote{Each major bankruptcy law of the United States has contained provisions for} The United States Constitution gives Congress the
power to enact uniform laws on the subject of bankruptcies. \(^3\) While states can enact insolvency laws in the absence of preemptive federal legislation, \(^4\) the Contracts Clause of the Constitution\(^5\) precludes the states from imposing discharges on creditors with respect to debts incurred before the date of enactment of the insolvency laws. \(^6\)

The concept of business reorganization is significantly different from that of business liquidation. The goal of reorganization is to preserve the enterprise as a going concern\(^7\) where its reorganization value exceeds its liquidation value. \(^8\) In the United

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3. The Bankruptcy Clause of the Constitution provides that "The Congress shall have Power . . . To establish . . . uniform Laws on the subject of Bankruptcies throughout the United States." U.S. CONST., art. I, § 8, cl. 4.


7. "Going concern" refers to a business whose capital and labor resources remain largely intact. Courts have long recognized that a business may have a going concern value or bonus in excess of its value on liquidation. See, e.g., Pacific Tel. & Tel. Co. v. Whitcomb, 12 F.2d 279 (W.D. Wash. 1926), aff'd, 276 U.S. 97 (1928); East Bay Water Co. v. McLaughlin, 24 F. Supp. 222, 226 (N.D. Cal. 1938) (going concern value is the value which inheres in a plant, its business established, as distinguished from one that has yet to establish its business).

The purpose of a business reorganization case, unlike a liquidation case, 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. The premise of a business reorganization is that assets that are used for production in the industry for which they were designed are more valuable than those same assets sold for scrap. . . . It is often more economically efficient to reorganize than to liquidate, because it preserves jobs and assets.

States, the concept of business reorganization has been appended to the business liquidation laws\(^9\) in order to take advantage of the Bankruptcy Clause of the Constitution.\(^{10}\) While the legality of this law is taken for granted today, at one time it was unsuccessfully challenged as violative of the Constitution.\(^{11}\)

**B. Implications For Defining Success.**

Thus in analyzing the scope of business bankruptcy cases, we must consider both business liquidation cases and business reorganization cases, even though they are very different.\(^{12}\) Not surprisingly, the paradigms for success in these two types of

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\(^9\) Unless creditors agree to take less, the Bankruptcy Code requires creditors to receive at least as much under a chapter 11 plan as they would receive in a chapter 7 liquidation case of the debtor. 11 U.S.C. § 1129(a)(7)(A)(ii) (1994).

\(^9\) See, e.g., Railroad Reorganization Act of 1933, ch. 204, 47 Stat. 1467, 1474, enacted as § 77 of the Bankruptcy Act.

\(^10\) See supra notes 1, 3.


The fundamental and radically progressive nature of these extensions becomes apparent upon their mere statement; but all have been judicially approved or accepted as falling within the power conferred by the bankruptcy clause of the Constitution. Taken altogether, they demonstrate in a very striking way the capacity of the bankruptcy clause to meet new conditions as they have been disclosed as a result of the tremendous growth of business and development of human activities from 1800 to the present day. And these acts, far-reaching though they may be, have not gone beyond the limit of congressional power; but rather have constituted extensions into a field whose boundaries may not yet be fully revealed.

294 U.S. at 671, 55 S. Ct. at 604.

\(^12\) Although cases filed under chapter 7 of the Bankruptcy Code generally result in liquidation of the business and cases filed under chapter 11 of the Bankruptcy
cases differ in many respects as well. Yet a common question applicable in both contexts is whether success should be defined in financial terms, by measuring the return to creditors and owners of the business, or in broader societal terms. This paper opts for the broader measure, which includes nonfinancial variables and costs of the business that are externalized.\(^\text{13}\)

This broader measure compounds our difficulty in defining success in business bankruptcies. As demonstrated below, the definitional process is complex and nonlinear,\(^\text{14}\) giving rise to different perceptions of success depending on the perspective.

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\(^\text{13}\) Code generally are intended to reorganize the business, the opposite can occur. Indeed, the Bankruptcy Code specifically permits a chapter 11 plan to provide for the sale of all or substantially all of the assets of the estate, with the proceeds to be distributed to creditors. 11 U.S.C. § 1123(a)(5)(D), (b)(4) (1994). It is also possible to have a reorganizing chapter 7 case where the trustee chooses to operate the business and sell it as a going concern. 11 U.S.C. § 721 (1994). See, e.g., In re Heisinger Resources, Ltd., 67 B.R. 378, 384 (C.D. Ill. 1986) (affirming decision of bankruptcy judge to allow trustee to operate business in order to maximize receipts on sale of business). Thus the difference between liquidation and reorganization cases is not as sharp as might first appear. Indeed, a large reorganization case almost always involves some degree of liquidation of assets. See Lynn M. LoPucki & William G. Whitford, Patterns in the Bankruptcy Reorganization of Large Publicly Held Companies, 78 CORNELL L. REV. 597, 605, 612 (1993) [hereinafter LoPucki & Whitford, Patterns]. For the sake of simplicity, however, this article assumes that chapter 7 cases are liquidations and chapter 11 cases are reorganizations.

Nonfinancial variables such as fairness, integrity, and attractiveness of the bankruptcy system are all important measurements of the success of the business bankruptcy system. See infra text accompanying notes 87, 90. By the same token, evaluating the externalities imposed by the business on society is equally important. See infra note 79 and accompanying text. In fact, maximizing total social value of the debtor firm can be understood as an efficiency concern. See Richard V. Butler & Scott M. Gilpatrick, A Re-Examination of the Purposes and Goals of Bankruptcy, 2 AM. BANKR. INST. L. REV. 269 (1994).

\(^\text{14}\) See Lawrence Ponoroff, Enlarging the Bargaining Table: Some Implications of the Corporate Stakeholder Model for Federal Bankruptcy Proceedings, 23 CAP. U. L. REV. 441, 452 (1994) ("[I]t would be specious to assume that any particular model or general legal theory can satisfactorily explain a subject as complex as bankruptcy."). Some commentators have recognized that decisions in bankruptcy cases are often made quickly within incomplete information. Mark E. MacDonald et al., Chapter 11 as a Dynamic Evolutionary Learning Process in a Market with Fuzzy Values, 1993-94 ANN. SURV. BANKR. L. 1, 22-25 (William L. Norton, Jr. ed.).
from which the issue is addressed. As noted above, the matter is complicated further by the significant differences between a chapter 7 liquidation case and a chapter 11 reorganization case, either of which can be a business bankruptcy. But before we consider applying the concept of success to the context of business bankruptcies, it is worth a brief detour to consider the abstract meaning of success *vel non*.

II. The General Meaning Of "Success."

This part explores the general meaning of success in lay and philosophical contexts. After briefly examining the concept of success from a law-and-economics perspective, this part concludes by discussing chaos theory as a model to define success in business bankruptcies.

The presence of fuzzy variables and imperfect information, when coupled with a system that is sensitively dependent on initial conditions, creates a classic chaotic model where similar cases generate different outcomes on a regular basis. *Id.* at 10-16. Although some commentators believe that the process and outcome in bankruptcy cases are or will be predictable, the contrary may well be true. *Compare* Lisa Hill Fenning, *The Future of Chapter 11: One View from the Bench*, 1993-94 ANN. SURV. BANKR. L. 113, 114-15, 117-18 (William L. Norton, Jr. ed.) (predicting the development of a typology of 5 or 6 major kinds of cases with characteristic life cycles and indicators of success or failure) *with* LoPucki & Whitford, *Patterns, supra* note 12, at 612 ("There is no stereotypical pattern for a Chapter 11 case involving a large, publicly held company.") *and* Elizabeth Warren, *Bankruptcy Policymaking in an Imperfect World*, 92 Mich. L. Rev. 336, 360 (1993) [hereinafter Warren, *Bankruptcy Policymaking*] (noting that the failure of theories to yield consistently predictable answers does not undercut the progress made by identifying normative goals of the bankruptcy system).

Bankruptcy is a complex process involving many different players with different perspectives. Debtors, managers, preferred shareholders, common shareholders, oversecured creditors, undersecured creditors, unsecured creditors, tax creditors, environmental creditors, tort creditors, contract creditors, trade vendors, employees, judges, administrators, attorneys, trustees, governmental units, and scholars may all bring different perspectives to the corporate bankruptcy case. For a discussion of the goals and incentives of several of these players, see *infra* parts III.B and IV.B.
A. Lay And Philosophical Notions Of Success.

The layperson thinks of success as the achievement of a desired outcome or end. And at least one prominent bankruptcy judge has adopted this approach, defining success as "the achievement of the results sought, or the avoidance of the results unwanted, by the debtor at the time of filing." While it might be appropriate to adopt this norm from the perspective of both the debtor and Western culture, it is worth examining alternative concepts of success throughout the ages.

Michael Devitt identifies four different concepts of success as follows:

Individual success: the success of an individual organism in satisfying its needs and fulfilling its desires.
Species success: the success of a species, including success in surviving.
Theoretical success: the success of a theory at the observational level: observational success.
Scientific progress: the success of scientists in getting better and better theories.

Of these, it is clear that bankruptcy law is neither a species nor a scientist. Although some commentators have analogized the bankruptcy estate to an individual living organism, the bankruptcy system itself does not have needs and desires to fulfill, apart from those prescribed by Congress and interpreted by the courts. Thus, it

\[16\] Indeed, this approximates the definition of "succeed" or "success" in the common dictionary. E.g., MERRIAM-WEBSTER'S COLLEGIATE DICTIONARY 1175 (10th ed. 1993).


\[18\] Michael Devitt, Does Realism Explain Success?, 41 REVUE INTERNATIONALE DE PHILOSOPHIE 29, 30 (1987).

\[19\] Chapter 11 creates a new artificial entity, the debtor in possession/estate. Like all other entities, biological and artificial, it must eat, internally communicate, decide what it must do to survive within the constraints of Chapter 11, and decide how its structure must be constructed after Chapter 11 (both sinew and decision system) to hunt, feed, survive, and possibly reproduce.

MacDonald et al., supra note 14, at 4.
appears to this author that theoretical success is the best mechanism for evaluating business bankruptcy.

We must determine the extent to which the business bankruptcy system is successful at the observational level. As such, it is fair for us to inquire to what extent the system is achieving the objectives it is designed to accomplish. Yet there may be deeper philosophical issues that permeate the concept of success.

Philosophers do not appear to have devoted much energy to defining the concept of success, but a few have ventured thoughts on the topic. The ancient Chinese philosopher Chuang Tzu embraced a philosophy of freedom from the world's ills. In describing the World of Men, Chuang Tzu notes the importance of the fasting of the mind and making the will one; listening with the spirit leads to emptiness which waits on all things. In this context, Chuang Tzu quotes Confucius as saying, "[h]ave no gate, no opening, but make oneness your house and live with what cannot be avoided. Then you will be close to success." It appears that Chuang Tzu, or at least Confucius, regards success as achieving the oneness of spirit through the fasting of the mind. In this respect, success is very much having attained a desired outcome or result, or at least having entered into a desired state. Thus once we have identified the

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20 This article does not presume to present anything more than a philosophical overview of success. Although many philosophers use the word "success," they seldom define or describe it.

21 Chuang Tzu or Master Chuang is thought to have lived about 370-301 B.C. during the latter stages of the Chou Dynasty, though it is through the book Chuang Tzu, which may have been authored by many minds, that the philosophy was expressed. See CHUANG TZU 1-3 (Burton Watson trans., Colum. U. Press 1964).

22 Id. at 54.

23 Id.
desired outcome or result, we can define success as the achievement of the outcome or result.

Indeed, other writers and philosophers have analyzed success by focusing on the extent to which an outcome is achieved. For example, Emerson wrote that "[s]uccess consists in close appliance to the laws of the world, and since those laws are intellectual and moral, an intellectual and moral obedience." This view recognizes that success may be aspirational rather than determinable. We may not be capable of obeying intellectual and moral laws absolutely, but if we observe those laws carefully, we may be able to attain success.

Schopenhauer notes that success can be incremental:

Every piece of success has a doubly beneficial effect on us when, apart from the special and material advantage which it brings[,] it is accompanied by the enlivening assurance that the world, fate, or the daemon within, does not mean so badly with us, nor is so opposed to our prosperity as we had fancied; when in fine, it restores our courage to live.

Attaining preliminary objectives and milestones that fall short of the overall desired outcome or end can constitute pieces of success.

Some writers thus focus on identifying preliminary goals that must be achieved as preconditions to success. For example, when Theodore Dreiser asks Marshall Field to identify "the first requisite for success in life," Field replies, "[t]he qualities of honesty, energy, frugality, integrity, are more necessary than ever to-day, and there is no

success without them."26 We might use the same criteria to evaluate success of a corporate bankruptcy system.27

B. Economic Models And Success.

Some traditional law-and-economics academics might analyze the success of any system, including the business bankruptcy system, in the context of the perfect market, a world without transaction costs, information asymmetries, or ambiguous property rights.28 These academics focus primarily on efficiency, or eliminating inefficiency.29 Although the theory of law and economics provides a lens to forecast what people should do in a particular situation, it is a poor framework for explaining what actually happens.


27 See infra text accompanying note 91.


For a critique of this fantasy world, see, e.g., Warren, Bankruptcy Policymaking, supra note 14, at 380-82; Donald R. Korobkin, Rehabilitating Values: A Jurisprudence of Bankruptcy, 91 COLUM. L. REV. 717, 740-44 (1991) [hereinafter Korobkin, Rehabilitating Values]. See also Butler & Gilpatric, supra note 13, at 275 ("Most importantly, Chameleon Equity and Contingent Equity [,as developed in the law-and-economics literature,] both depend critically upon the existence of perfect markets and the absence of transaction costs.").

Traditional law-and-economics analysis suffers from its unrealistic assumptions of perfect markets and zero transaction costs. See Jean Braucher, Bankruptcy Reorganization and Economic Development, 23 CAP. U. L. REV. 499, 503 (1994). Bankruptcy laws exist precisely because markets are imperfect and splitting up the capital and labor resources of a business is fraught with transaction costs. See Butler & Gilpatric, supra note 13, at 282-84.

29 See generally JACKSON, supra note 28, Baird, Uneasy Case, supra note 28.
The deficiencies in traditional law-and-economics theory have led some academics to enhance or revise the theory to account for externalities or other economics-based concepts to account for the inexplicable.\textsuperscript{30} For example, some modern rational-actor economists would enhance their theory to select more objective preliminary goals such as minimization of the sum of transaction costs and the costs of coordination failures.\textsuperscript{31}

Yet our challenge remains to move past law and economics to a theory that is descriptive of reality as well as coherent. Some of the brightest scholars have recognized that the answer may lie in integrating chaos theory into the blend.\textsuperscript{32}


\textsuperscript{31} See Robert C. Ellickson & Charles DiA. Thorland, Ancient Land Law: Mesopotamia, Egypt, Israel 2 (November 1, 1995)(unpublished manuscript, on file with author) (identifying these goals in the context of property institutions).

C. Chaos Theory As A Model To Define Success.

The efforts of law-and-economics scholars to define success in terms of profit maximization or cost minimization (to the exclusion of intangible social mores) are subject to criticism.\textsuperscript{33}

Exactly that callousness to abstract justice is the sinister feature and, to me as well as to you, the incomprehensible feature of our U.S. civilization . . . understandable in onlooking citizens only as a symptom of the moral flabbiness born of the worship of . . . SUCCESS. That—with the squalid cash interpretation put on the word success—is our national disease.\textsuperscript{34}

\textsuperscript{33} Some legal commentators recognize the importance of "recognizing noneconomic outcomes as independent values." Korobkin, \textit{Rehabilitating Values}, supra note 28, at 741. See Ponoroff, \textit{supra} note 14, at 455 ("The collapse of a business enterprise implicates a broad range of diverse interests beyond the interests of those persons with cognizable state law claims against the assets of a business."). Even a business person might consider profit maximization less important than \textcolor{red}{defeating competitors, advancing technology, or overcoming other obstacles}. See RUPERT C. LODGE, \textcolor{red}{PHILOSOPHY OF BUSINESS} 92 (1945)(quoting and condensing various passages from W.T. HUTCHINSON, CYRUS HALL MCCORMICK (1935)). See also Duncan Kennedy, \textcolor{red}{Cost-Benefit Analysis of Entitlement Problems: A Critique}, 33 STAN. L. REV. 387, 445 (1981) ("It is nonetheless unlikely that the enthusiasm for efficiency will abate, given its enormous apologetic usefulness . . . . of generating an apparently 'scientific' justification for liberal reformist proposals.").

\textsuperscript{34} Letter from William James to H.G. Wells (Sept. 11, 1906), in 2 THE LETTERS OF WILLIAM JAMES 259, 260 (Henry James ed., 1920) (emphasis in original).
In order to avoid this disease, we must formulate a norm of optimal social benefit that includes honesty, justice, and other soft variables\textsuperscript{35} worthy of consideration.\textsuperscript{36} We may find it difficult to quantify or calibrate certain soft variables. The problems that these soft variables might create in the measurement of success should not prevent their inclusion in our analysis, even if a necessary consequence is that the determination of success will be more subjective or less determinable than some theoreticians would desire.\textsuperscript{37} Rather, we should embrace turbulence and uncertainty as part of life and accommodate our theories accordingly.

\textsuperscript{35} A soft variable is one that defies easy measurement or one whose evaluation is necessarily subjective. \textit{See} Laurence H. Tribe, \textit{Trial by Mathematics: Precision and Ritual in the Legal Process}, 84 \textsc{Harv. L. Rev.} 1329, 1361-65 (1971) ("If you can't count it, it doesn't exist."). \textit{Id.} at 1381. Professor Tribe observes that "[r]eadily quantifiable factors are easier to process—and hence more likely to be recognized and then reflected in the outcome—than are factors that resist ready quantification. The result, despite what turns out to be a spurious appearance of accuracy and completeness, is likely to be significantly warped and hence highly suspect." \textit{Id.} at 1362. Dean Robert Scott has analyzed this phenomenon in the context of law and economics: "While [law and economics] illuminates brightly everything within its focus, it necessarily casts the periphery in shadow. In short, it is that part of the legal structure that is not susceptible to economic analysis—especially the concerns of distributional equity . . . that gives us pause." Scott, \textit{supra} note 32, at 344.

\textsuperscript{36} The strength of our democracy is that it tempers the market by managing the tension between the efficient allocation of resources and the fair distribution of wealth. Braucher, \textit{supra} note 28, at 507 (discussing ALBERT O. HIRSCHMAN, RIVAL VIEWS OF MARKET SOCIETY AND OTHER RECENT ESSAYS 105-139 (1986)). Corporate bankruptcy, as a legal institution within our democracy, fits this model well. See Frank H. Easterbrook, \textit{Is Corporate Bankruptcy Efficient?}, 27 \textsc{J. Fin. Econ.} 411, 413-14 (1990) ("Legal institutions endure either because they are efficient or because they redistribute wealth to concentrated, politically effective interest groups.").

\textsuperscript{37} Indeed, consideration of these soft variables must be part of the value-based decisions that are necessarily made in discussing or attempting to define success in corporate bankruptcy. \textit{See} Korobkin, \textit{Rehabilitating Values}, \textit{supra} note 28, at 768 ("Bankruptcy law creates conditions for a discourse in which the problem of financial distress may be confronted on its own moral, political, personal, social, and economic terms."). Although some law-and-economics advocates would contend that an efficiency analysis avoids these considerations, it is "perfectly obvious that the efficiency of cost-benefit calculus is simply a language for
Chaos theory provides a useful vehicle to formulate and evaluate notions of success. Generally speaking, chaos attempts to explain "orderly disorder created by simple processes." There are several basic elements of chaos theory. Sensitive variations in initial conditions can produce dramatic changes in outcomes, making prediction highly unreliable. Nonlinear systems can give rise to multiple possible solutions, and the feedback that changes the system alters the rules under which future outcomes are determined. Strange attractors within the system influence the carrying on political or ethical discussion, rather than a way of discovering facts about the external world that can then be politically or ethically assessed (or ‘balanced’ against things like distributational equity).” Kennedy, supra note 33, at 411 (emphasis in original; footnote omitted). Balancing the quantifiable aspects of success with its unquantifiable aspects is an essential part of the definition of success.

JAMES GLEIK, CHAOS: MAKING A NEW SCIENCE 266 (1987).

The basic elements of chaos theory have been discussed in numerous sources. See generally, id.; HARRIET HAWKINS, STRANGE ATTRACTIONS: LITERATURE, CULTURE AND CHAOS THEORY (1995); CREEDY & MARTIN, supra note 32.

Scott, supra note 32, at 348. ("[A]ll systems are chaotic, in the sense that they are subject to irregularities that make predictions of outcomes in particular cases impossible.") For an example in bankruptcy case law, where the same panel of the court of appeals reached sharply opposed results on similar facts, compare Norwest Bank Nebraska, N.A. v. Tveten, 848 F.2d 871 (8th Cir. 1988) (sustaining objection to discharge on the basis that doctor's exemption planning was fraudulent) with Hanson v. First Nat'l Bank, 848 F.2d 866 (8th Cir. 1988) (allowing farmer to convert property into exempt property on the eve of bankruptcy). See also Panuska v. Johnson (In re Johnson), 880 F.2d 78, 84 (8th Cir. 1989) (holding that size of homestead exemption is irrelevant in determining the doctor’s fraudulent intent, but remanding to determine whether there is extrinsic evidence of fraud in the doctor's conversion of property into other kinds of exempt property).

See CREEDY & MARTIN, supra note 32, at 87-98 (demonstrating multiple equilibria in simple exchange models).

In this article, "feedback" is used in the sense of positive recursion, whereby a system may be induced to change its response to a particular problem based on its evaluation of internal and external responses to previous problems.

In the bankruptcy context, the "recursion or reiteration caused by the constant
likelihood of future outcomes even though a particular series of outcomes may never be repeated.\textsuperscript{45}

need to go back and forth between federal and state principles" produces a feedback effect that "is likely to result in a bounded chaotic set." MacDonald et al., \textit{supra} note 14, at 20. That is, although the specific outcome within the set of possibilities for a particular bankruptcy case may be difficult or impossible to predict, the realm of possible outcomes is determinable.

A "strange attractor" is a magnetic basin or point of instability that is a source of information as well as disorder. HAWKINS, \textit{supra} note 39, at 20. While certain outcomes within a system may be predictable, as we approach the boundaries of tension between strange attractors we see unpredictability, complexity, and chaos.

In a manner of speaking, this is why hard cases make bad law. Hard cases invariably involve fact patterns that implicate two or more conflicting principles of law. The \textit{Hanson}, \textit{Johnson}, and \textit{Tveten} cases, referenced \textit{supra} in note 40, are good examples. Consider these three strange attractors: (1) The honest individual debtor is entitled to a discharge of debts and a fresh start; (2) The debtor who defrauds creditors is not entitled to a discharge of debts and a fresh start; and (3) Transferring assets on the eve of bankruptcy is a badge of fraud. Based on a given set of facts involving the debtor's transfer of nonexempt assets into exempt assets, a court that is influenced by these strange attractors could reach one of two alternative conclusions: the transfer is (a) a fraud on creditors that warrants denial of discharge; or (b) legitimate exemption planning designed to facilitate the honest debtor's fresh start. As the transfer takes place closer in time to the filing of the bankruptcy petition and involves greater and greater amounts of property, the fact pattern moves from the outcome in (b) toward the outcome in (a). Cases with facts at the extremes are easy to predict; cases with facts at the border between these competing strange attractors are difficult if not impossible to predict.

Some commentators posit that there are less than a dozen "great rules" which will act as the principal Strange Attractors [in bankruptcy law]. These rules include:

1. Bankruptcy abhors forfeitures.
2. The estate should be maximized.
3. Bankruptcy will follow state law property and priority rules or adequately protect those rights.
4. Bankruptcy prefers more equal distributions over all or nothing distribution.
5. Bankruptcy prefers reorganization to liquidation.
7. In bankruptcy, everyone should leave a little dissatisfied.
8. Bankruptcy will punish a refusal to bargain.
9. Minority positions can be bound by the will of the majority.
10. Bankruptcy favors consensus.
Although our inability to predict a specific outcome with a high degree of certainty may be unsettling, the beauty of chaos theory is that it enables us to identify large patterns. Even though the patterns are complex, they are nevertheless bounded in many contexts. Recognizing these patterns can yield insights that apply across fields, including the field of business bankruptcy. We can thus use the lens of chaos to help define success in business bankruptcy.

Even though chaos theory might be helpful in assisting us to identify patterns, it offers us incomplete guidance in resolving the balance between quantifiable and unquantifiable variables. This limitation of chaos theory is not disabling, provided we formulate an heuristic to overcome it. If almost every important factor of success is quantifiable, perhaps we can use a utilitarian analysis to determine success, subject to a second look or adjustment to account for unquantifiable factors. On the other hand, if important aspects of success are unquantifiable, then we should embrace a dual system where the quantifiable and unquantifiable elements are given equal dignity in defining success. In order to determine which heuristic to adopt, we must first identify the basic elements of success in the business bankruptcy system.

11. Bankruptcy requires that participants act in good faith.
12. Bankruptcy follows statutory language.

MacDonald et al., supra note 14, at 79-80. It is the tension among these sometimes conflicting principles that causes the complexity at the border and the sensitive dependence on initial conditions that are characteristic of chaos. Cf. Karl N. Llewellyn, Remarks on the Theory of Appellate Decision and the Rules or Canons About How Statutes Are to Be Construed, 3 VAND. L. REV. 395 (1950) (noting themes in tension in appellate decisions and identifying 28 pairs of opposing canons of statutory construction).
III. Defining Success In Chapter 7 Business Liquidation Cases.

This part describes the basic elements of the chapter 7 liquidation process and explores alternatives to chapter 7. We examine the players in a chapter 7 business liquidation case and analyze their competing and conflicting goals. Part III concludes by formulating a definition of success for chapter 7, in light of the turbulence created by these conflicting goals. The analysis proceeds beyond traditional statistical measures of success to incorporate unquantifiable variables, such as justice, into the definition of success.

A. The Basics Of The Chapter 7 Process And Alternatives.

This section describes the basics of the chapter 7 liquidation process and discusses some of the alternatives to chapter 7. For purposes of analysis, this article defines a "business liquidation case" as a case under chapter 7 of the Bankruptcy Code involving a corporate or partnership debtor that operates or operated a business.

1. Summary Of The Liquidation Process.

By comparison to the chapter 11 business reorganization case, the chapter 7 business liquidation case is fairly straight-forward. At the commencement of the case, the management of the business is ousted and a trustee is appointed (or

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46 As set forth below, a chapter 11 reorganization requires numerous predictions about the future with respect to the viability of the business and its potential earning power. See infra notes 125, 133 and accompanying text. Valuations may be fuzzy because of uncertain uses and court-determined values rather than market-determined values. By contrast, in chapter 7, the fate of the business is known. The business will be liquidated, although the method of liquidation may be uncertain. Also, there is no issue whether the debtor gets or deserves a fresh start. Moreover, in chapter 7, the trustee is in full control; creditors have little say and do not vote on a plan. Thus there are fewer variables to consider and the process is less complex than in chapter 11, where the business may undergo reorganization, liquidation, or some combination of the two.
The goal of the trustee is to reduce the assets of the estate to money "as expeditiously as is compatible with the best interests of parties in interest." The trustee may also exercise avoiding powers to avoid preferences, fraudulent transfers, and the like to promote equality of distribution among unsecured creditors. Commentators often assume that the purpose of these powers is to maximize value for the debtor's unsecured creditors. The value-maximization goal and equality-of-distribution principle are strong "strange attractors" in chapter 7.

2. Alternatives To Chapter 7 Liquidation.

Not all businesses meet their demise in chapter 7. Sometimes the debtor permits creditors to exercise their remedies under nonbankruptcy law to dismember the business piecemeal. Then the debtor winds up and dissolves under nonbankruptcy law. Since the partnership or corporate debtor does not receive a discharge of its debts in chapter 7 and the debtor's responsible officers must be examined under

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50 Commentators assume it is desirable to sell the assets of a bankrupt company at the highest price possible. See Lynn M. LoPucki & William C. Whitford, Corporate Governance in the Bankruptcy of Large, Publicly Held Companies, 141 U. PA. L. REV. 669, 752 n.254 (1993) [hereinafter LoPucki & Whitford, Corporate Governance].

51 See supra notes 44-45.

52 As a matter of law, no partnership or corporate debtor is entitled to a discharge in
oath, the debtor's managers have little incentive to file a chapter 7 bankruptcy petition for the debtor. Instead, managers may cause the debtor to make a general assignment for the benefit of creditors. In fact, in states where general assignments for the benefit of creditors are popular, prudent practitioners do not file chapter 7 business liquidation cases unless the debtor's assets are fully encumbered and no assignee is willing to serve.

Every debtor must submit to an examination under oath concerning the circumstances of the bankruptcy. See 11 U.S.C. § 343 (1994). When the debtor is a partnership or corporation, the Bankruptcy Rules permit the court to designate a responsible officer of the debtor to testify under oath on the debtor's behalf. See FED. R. BANKR. P. 9001(5).

Many states provide for statutory or common law general assignments for the benefit of creditors. E.g., CAL. CIV. PROC. CODE §§ 493.010-493.060 (West 1979 & Supp. 1996). A general assignment is accomplished when a debtor transfers to an assignee all transferable assets not exempt from a money judgment; the assignment must be for the benefit of all of the debtor's creditors. See, e.g., id. § 493.010. See also Missouri-American Elec. Co. v. Hamilton-Brown Shoe Co., 165 F. 283, 288 (8th Cir. 1908).

Since a corporate or partnership debtor does not receive a discharge in a chapter 7 case, see supra note 52, the debtor's managers have little incentive to subject the business to the jurisdiction of the court, where they must supply detailed information about the business and answer questions under oath. If the debtor's assets are fully encumbered, the debtor's managers can allow the secured creditors to foreclose their liens or pursue nonbankruptcy remedies. Alternatively, the managers can commence a chapter 7 case for the debtor to alleviate creditor pressure and subject the assets to a public auction with the secured creditors' consent. See 11 U.S.C. § 363(f) (1994). In the author's experience, sometimes the debtor's secured creditors prefer the managers to initiate a chapter 7 case for the debtor so that the debtor's assets may be sold at a bankruptcy sale. See id.; FED. R. BANKR. P. 6004. From the secured creditors' perspectives, the bankruptcy sale might relieve them from liability they would have incurred if they conducted an improper foreclosure sale or took title to collateral contaminated with toxic waste. See U.C.C. § 9-507(1) (1972) (making secured party liable for improper disposition of collateral); United States v. Fleet Factors Corp., 901 F.2d 1550 (11th Cir. 1990) (holding foreclosing creditor liable as operator of environmentally contaminated property), cert. denied, 498 U.S. 1046, 111 S. Ct. 752 (1991).
B. The Players And Their Goals And Incentives.

This section discusses the players in chapter 7 and their goals and incentives. Our definition of success would be simplified if all players shared the common goal of maximizing the value of the chapter 7 estate. Regrettably, the chapter 7 process is nonlinear and multidimensional, because it may not be in the interest of each party in the system to act efficiently to maximize value for the whole or to distribute property of the estate equally.\(^\text{56}\)

1. The Debtor.

To simplify our analysis, this article assumes that the business debtor in chapter 7 is a partnership or corporation that will not be entitled to a discharge of its debts.\(^\text{57}\) Unless the estate is solvent,\(^\text{58}\) the debtor and its owners have little at stake in the outcome of the chapter 7 case other than the time they will devote to the process. Obviously, if the debtor were an individual proprietor, the debtor’s interest in obtaining a discharge\(^\text{59}\) and maximizing exemptions\(^\text{60}\) would create an enormous tension with the

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\(^{56}\) Traditional law-and-economics theory would look at the consequences of legal choices, label any suboptimal result as "inefficient" and seek to redesign the system to remove the inefficiency. See RICHARD A. POSNER, ECONOMIC ANALYSIS OF LAW 20-22 (3d ed. 1986). While it might be possible to make the liquidation system more efficient, the presence of turbulence and feedback in the liquidation system, as influenced by the presence and fuzziness of soft variables, makes a perfectly efficient system impossible. This reality has led some law-and-economics academics to settle for a system that approaches efficiency. See, e.g., Roe, supra note 32, at 662 (recognizing that path dependence makes economic systems inefficient but often left unchanged).

\(^{57}\) See supra note 52 and accompanying text.

\(^{58}\) If the liquidated value of the debtor’s assets exceeds the sum of its administrative expenses, liabilities, and postpetition interest, then the debtor is solvent and a surplus will be returned to the debtor. See 11 U.S.C. § 726(a)(6) (1994).

\(^{59}\) While a business debtor can sell its assets and dissolve, an individual debtor must
desires of secured creditors, unsecured creditors, and the trustee to maximize the value of the estate for the benefit of creditors.\textsuperscript{61} While not directly analogous, the discussion set forth below with respect to the chapter 11 discharge would apply to some extent to an individual proprietor in a chapter 7 business liquidation case.\textsuperscript{62}

\textsuperscript{60} In order to facilitate the individual debtor's fresh start, the Bankruptcy Code provides a complex scheme whereby the individual debtor can exempt certain property from the reach of most unsecured creditors. See 11 U.S.C. § 522 (1994).

\textsuperscript{61} For the individual debtor, obtaining a discharge and maximizing exempt assets are strong strange attractors in chapter 7 cases. The absence of these concerns in business cases simplifies the analysis somewhat.

\textsuperscript{62} See infra notes 139-140 and accompanying text.
2. **Secured Creditors.**

Secured creditors have liens encumbering certain assets of the estate.\(^{63}\) It is in their interest to maximize their own return, usually by obtaining their collateral or its proceeds as soon as possible. If the collateral will enhance the value of other assets in the estate, the secured creditors' goal may conflict with the desire of the trustee and unsecured creditors to maximize the residual bankruptcy estate. For example, the debtor might be in the business of selling watches.\(^{64}\) The trustee might desire to operate the business for a brief time to assemble watch movements and cases for sale as finished product rather than to sell the parts separately. If the machine necessary for assembly of the watches is subject to the lien of a secured creditor, but the inventory is not, the conflict is apparent. The secured creditor will want to liquidate its collateral as soon as possible, and the trustee and unsecured creditors will want to delay the secured creditor so that the estate can use the machine to assemble the watches.

3. **Unsecured Creditors.**

The goal of all unsecured creditors in a chapter 7 case is to maximize the distribution on their claims on a present-value basis. Although the goal of equality of distribution is a strong strange attractor in chapter 7 cases, the law does not treat all unsecured creditors equally. Social policies embedded in bankruptcy distribution rules

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\(^{63}\) A "lien" is defined as a "charge against or interest in property to secure the payment of a debt or the performance of an obligation." 11 U.S.C. § 101(37) (1994). Liens may be consensual, such as security interests or mortgages; imposed by statute, such as artisans' liens or tax liens; or imposed by courts, such as judicial liens or equitable liens. See 11 U.S.C. § 101 (36), (51), (53) (1994).

\(^{64}\) This example is mentioned in HOUSE REPORT, *supra* note 7, at 380, as a situation in which the court might authorize the trustee to operate the debtor's business in a chapter 7 case.
grant priority to certain unsecured claims and may subordinate other secured or
unsecured claims.\textsuperscript{65} In addition to the mandatory statutory avoidance or subordination
of certain claims, the Bankruptcy Code allows the court to equitably subordinate claims
where circumstances warrant.\textsuperscript{66} Creditors with different priorities may have competing
interests where the estate contains sufficient assets to pay senior creditors but
insufficient assets to pay subordinated creditors. Junior creditors might prefer the
trustee to delay liquidating assets, hoping that prices will rise to enhance the value of
the assets. If prices fall, the return to senior creditors might be less than what they
would have received in a prompt liquidation. Thus, to limit down side risk, senior
unsecured creditors might prefer the trustee to liquidate assets promptly. By the same
token, senior secured creditors might prefer to receive their collateral immediately, by
obtaining relief from the automatic stay to conduct foreclosure sales, in order to capture
any increase in value of their collateral above the amount of their claims.\textsuperscript{67}

\textsuperscript{65} See, \textit{e.g.}, 11 U.S.C. §§ 507(a), 724 (1994).


\textsuperscript{67} Secured creditors commonly acquire their collateral by bidding in their claims at
foreclosure sales, generating values that are so far below market values that the
foreclosure sales have been attacked as constructive fraudulent transfers. See,
\textit{e.g.}, Durrett \textit{v.} Washington Nat’l Ins. Co., 621 F.2d 201, 203-04 (5th Cir. 1980)
(holding that foreclosure sale that yielded 57\% of property’s fair market value
should be set aside), \textit{overruled by} BFP \textit{v.} Resolution Trust Corp., 114 S. Ct. 1757
(1994) (upholding regularly conducted, noncollusive real estate mortgage
foreclosure sale because consideration received is deemed to be exchanged for
reasonably equivalent value).
4. The Trustee.

As previously mentioned, the trustee is the legal representative of the chapter 7 estate and is charged with reducing the assets of the estate to money.\textsuperscript{68} Although the trustee is supposed to proceed with expedition to maximize the value of the estate, the theoretical goals of the chapter 7 liquidation case often conflict with the practical realities faced by private trustees administering hundreds or thousands of chapter 7 cases. Even though trustees are given several rights and powers to assist them in maximizing the value of the estate,\textsuperscript{69} the transaction costs of implementing those powers preclude their utilization in many circumstances. For example, the cost of researching, filing, and prosecuting a preference action to recover $700 might exceed the expected recovery to the estate.

5. The Bankruptcy Court.

The bankruptcy judge, clerk, and other court employees operate the chapter 7 court system. The willingness of the bankruptcy judge to devote time to chapter 7 litigation issues is a factor influencing the realities of chapter 7. The Administrative Office of the United States Courts evaluates clerks based in part on the speed with which cases are processed and closed.\textsuperscript{70} Therefore we can presume that the clerks of court, and presumably some judges, prefer cases to be processed expeditiously.\textsuperscript{71}

\textsuperscript{68} See supra notes 47 & 48 and accompanying text.

\textsuperscript{69} See supra note 49 and accompanying text.

\textsuperscript{70} The Administrative Office of the United States Courts is an agency in the judicial branch of government located in Washington, D.C. See 28 U.S.C. § 601 (1994). Under the supervision and direction of the Judicial Conference of the United States, the Director of the Administrative Office is charged, inter alia, with supervising the administration of the federal court system and the judicial branch of government. See 28 U.S.C. § 604 (1994). The Director is required to produce
6. The Office Of United States Trustee.

The Office of United States Trustee supervises the administration of chapter 7 cases and the trustees who administer the cases. The United States trustees (and estate administrators) are concerned with the efficiency and integrity of the system.

7. Congress.

Congress is interested in the chapter 7 process to the extent it consumes national resources. Even if chapter 7 provides benefits, because the system consumes resources, Congress must determine who funds the cost of the bankruptcy system.


For example, Judge Thomas Small instituted a procedure to put chapter 11 reorganizations on a fast track. See A. Thomas Small, Small Business Bankruptcy Cases, 1 AM. BANKR. INST. L. REV. 305 (1993). Based on the author's personal knowledge of the legislative process, certain bankruptcy judges were instrumental in obtaining amendments to the Bankruptcy Code to increase judicial involvement in case management. See 11 U.S.C. § 105(a)(2d sent.), (d) (1994). One purpose of actively involving judges in case management, even in the absence of any dispute, is to expedite cases. See, e.g., Fenning, supra note 14, at 122 ("By learning what the court expects of the case, the parties should be able to resolve the case far more expeditiously on their own.").


The United States trustee program is established throughout the United States except in North Carolina and Alabama. See 28 U.S.C. § 581(a) (1994). One court of appeals has held that the exclusion of North Carolina and Alabama from the United States trustee system violates the Bankruptcy Clause's requirement of uniformity. St. Angelo v. Victoria Farms, Inc., 46 F.3d 969 (9th Cir. 1995).

In North Carolina and Alabama, where United States trustees do not operate, estate administrators perform many of the same duties that United States trustees perform in the rest of the country. See supra note 72; Fed. R. BANKR. P. 9035.
Thus we have seen that the players in a chapter 7 liquidation case may have conflicting goals. These conflicting goals contribute to the instability and unpredictability of the chapter 7 system. As such, we must consider their impact on the definition of success.

C. Measuring Success In Chapter 7.

This section builds on the conflicting goals of the players to formulate a systemic definition of success in chapter 7. After considering traditional statistics-based measures of success, this section moves beyond statistics to incorporate more appropriate measures of success.

1. Success is A Matter Of Perspective.

The participants in the chapter 7 system are likely to have different perceptions of success of the system because their particular goals may differ. Some commentators might urge us to limit our focus to the participants with direct economic interests in the estate. This approach would lead us to solve a common-pool collective-action problem by engaging in a relatively simple value-maximization analysis coupled with a distribution to creditors based on their nonbankruptcy rights.74 But this type of analysis is insufficient to address conflicting goals of the players, because it ignores broader social aspects of the chapter 7 system, such as whether the system is just, that might be important to satisfy the goals of some players. A broader focus on the maximization of social value is necessarily more complex and imprecise, but chaos theory can help us overcome (or at least manage) these obstacles. For reasons

74 See, e.g., Jackson, supra note 28, at 7-19.
discussed below, this article opts to evaluate the chapter 7 system from the broader measure of maximizing justice and value to society.

2. Statistics-Based Measures.

a. Absolute Economic Returns.

Historically, commentators have measured the success of straight bankruptcy or liquidation cases by the dollar return to unsecured creditors.\textsuperscript{75} By measuring the length of the case, the percentage of the estate consumed by administrative expenses, the percentage of the estate distributed to unsecured creditors, and the relative percentage dividend received by unsecured creditors, academicians and bureaucrats have tried to quantify success in the chapter 7 context.

Measurement of these statistics in a chapter 7 context can be somewhat meaningful, since the data may provide clues that lead to improvement of the system.\textsuperscript{76} For example, if cases are taking longer to administer in some districts than in others, it

\textsuperscript{75} According to Professor LoPucki, unsecured creditors receive nothing on their claims in 80% of business liquidation cases and only 4.5%, on average, of the allowed amount of their claims in the remaining 20% of such cases. Lynn M. LoPucki, A General Theory of the Dynamics of the State Remedies/Bankruptcy System, 1982 Wis. L. Rev. 311, 311. (When a proof of claim is filed or deemed filed, it is deemed allowed unless a party in interest objects; if an objection is filed, the court determines whether, and in what amount, to allow the claim. See 11 U.S.C. §§ 501, 502, 1111(a) (1994); Fed. R. Bankr. P. 3001-3007.) More recent data support this finding. See Michelle J. White, Bankruptcy Liquidation and Reorganization, in HANDBOOK OF MODERN FINANCE E7-1, E-34 (Dennis E. Logue ed., 1995)(finding average payout of 4% on unsecured claims in 90 small business liquidation cases).

might be because trustees are overworked. On the other hand, it might be because
trustees in those districts are incompetent or lack motivation to process cases rapidly.77

b. Relative Economic Returns.

The absolute timeliness and magnitude of proceeds distributed in chapter 7
liquidation cases, standing alone, are insufficient measures of success. We should
examine the speed and percentage return in chapter 7 relative to both alternatives to
chapter 7 and a more efficient chapter 7. How much more could be distributed if
trustees would conduct investigations to recover assets that are secreted or fraudulently
transferred? What are the transaction costs of conducting such an investigation? How
well suited is the federal legal system to pursuing these assets? Unless these
questions are answered, we have less than a complete universe of information with
which to analyze the "success" of chapter 7, even assuming we wish to measure it
solely from the perspective of monies distributed to unsecured creditors.


Of course, from a societal perspective, the return to unsecured creditors only
begins to measure the success of the chapter 7 process. To facilitate our evaluation of
the impact of chapter 7 business liquidation cases on society, the concept of ultimate

77 Former bankruptcy judge Jack Ayer believes that chapter 7 should be abolished
so that businesses can liquidate under a debtor in possession in chapter 11. John
contends that abolishing chapter 7 will help "to simplify our analysis and clarify our
goals. Once we get rid of Chapter 7, we can see the real purpose of corporate
bankruptcy which is: to maximize the value of the asset pool for everyone . . . ." Id. at 4. Although Ayer's argument is provocative, he ignores the relative cost of
chapter 11 as compared to chapter 7. In chapter 7 there is no plan and creditors
do not vote. Cf. infra notes 126-133 and accompanying text (explaining plan and
vote in chapter 11). With the loss of democracy in chapter 7, we gain a saving in
cost.
success should include sociological, political, and economic externalities in addition to the internal economic factors described above. The Bankruptcy Rules suggest that bankruptcy should be just, speedy, and inexpensive. These three factors can provide a framework for our further definition of success in business bankruptcies. While speed and expense can be quantified in economic terms, justice cannot.

a. A Just System.

We can begin to measure the success of chapter 7 by questioning whether the distributive rules of chapter 7 are just and fair. Our examination should focus on the internal distribution rules of chapter 7 as well as the relative distributive rules under nonbankruptcy law. The priority and subordination schemes for chapter 7 cases have been established by Congress in sections 507, 510, 724, and 726 of the Bankruptcy Code. Although this bankruptcy distribution scheme does distort the pattern of distribution that would otherwise take place under nonbankruptcy law, that distortion is

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78 For example, chapter 7 partially eliminates an externality by accounting for the rights of some parties who would not have an immediate right to payment if the debtor were to liquidate under state law. See 11 U.S.C. §§ 101(5), 502(c) (1994) (defining "claim" to include unliquidated and contingent claims and providing for their estimation in bankruptcy cases); Warren, Bankruptcy Policymaking, supra note 14, at 354-56. Chapter 7 is also designed to minimize losses to the general public when a business fails. Id. at 361-68. But it cannot be denied that liquidating a business imposes external costs on employees, customers, suppliers, and other parties who have a relationship with the debtor that will be ended on liquidation. See Butler & Gilpatrick, supra note 13, at 281-83 (recognizing that external going concern value is lost in liquidation).


80 See 11 U.S.C. § 507 (1994) (establishing priorities for, inter alia, administrative expenses, wages, child support, alimony, and unsecured tax claims); id. § 510 (permitting contractual and equitable subordination of claims); id. § 724 (governing distribution of proceeds of property securing a tax lien and subordinating penalty liens); id. § 726 (governing distribution of property of the estate).
not troubling to this author. In particular, where a bona fide bankruptcy policy reason exists to override state law, the Supremacy Clause gives Congress the power it needs to impose the result. Indeed, the paradigm of equality of distribution among similarly situated creditors is just such an overriding collective principle. In analyzing whether the chapter 7 system is successful, we should determine whether departures from the norm of equality are fair and just. Certain federal priorities are designed to internalize

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81 The principle that bankruptcy law should not distort nonbankruptcy rights is another strange attractor for both chapter 7 and chapter 11. In part, the principle is designed to neutralize the inducement that some parties would have to file voluntary or involuntary bankruptcy petitions if their rights would be improved in bankruptcy. Courts have articulated this principle in construing bankruptcy law and policy. E.g., Butner v. United States, 440 U.S. 48, 55, 99 S. Ct. 914, 918 (1979) (whether a mortgagee has a perfected interest in rents is determined by nonbankruptcy law "to prevent a party from receiving 'a windfall merely by reason of the happenstance of bankruptcy.") (quoting Lewis v. Manufacturers Nat'l Bank, 364 U.S. 603, 609, 81 S. Ct. 347, 350 (1961)). Yet this principle often will be cast aside when a supervening bankruptcy principle or strange attractor, such as rehabilitation of a troubled company, is implicated. E.g., United States v. Whiting Pools, Inc., 462 U.S. 198, 207, 103 S. Ct. 2309, 2314-15 (1983) ("In effect, [the Bankruptcy Code] ... grants to the estate a possessory interest in certain property of the debtor that was not held by the debtor at the commencement of the reorganization proceedings.").

82 U.S. CONST., art. VI, cl. 2.


84 Except for the payment of claims entitled to priority under section 507 of the Bankruptcy Code, all timely filed unsecured claims with similar legal rights are entitled to share ratably in a chapter 7 case. 11 U.S.C. § 726(a)(2) (1994). This fundamental norm is acknowledged as an appropriate collective distribution rule, as opposed to the race of diligence under state law. See Union Bank v. Wolas, 502 U.S. 151, 161, 112 S. Ct. 527, 532-33 (1991); Warren, Bankruptcy Policymaking, supra note 14, at 352-53.
the cost of business losses; the eighth priority granted to unsecured tax claims is an example.\textsuperscript{85} Regrettably, the growing list of federal priorities is the result of lobbying by special interests rather than a reasoned congressional policy regarding a fair distribution scheme.\textsuperscript{86}

Even if the priority scheme were theoretically perfect, however, our measurement of success should embody social factors such as the degree to which a collective distribution scheme is beneficial in a civilized society. We can begin to measure the relative benefits of the collective chapter 7 liquidation system by comparing its results with results that would occur if chapter 7 did not exist. Clearly, one of the reasons bankruptcy law overrides "grab law" pertains to "fairness" rather than economic justification.\textsuperscript{87} Another reason for equal distribution is the suboptimal economic allocation that results from grab law, where imperfect information and

\begin{footnotesize}
\begin{enumerate}
  \item[85] 11 U.S.C. § 507(a)(8) (1994). See Warren, Bankruptcy Policymaking, supra note 14, at 361-63. By granting the government priority for its involuntary tax claims, the Code shifts the burden of the debtor's tax liabilities from taxpayers in general to the debtor's unsecured creditors. To the extent taxes are costs of doing business, the priority internalizes this cost when assets are available to pay the taxes in full.
  \item[86] It is difficult to justify priorities for grain merchants and United States fishermen on any other basis. See 11 U.S.C. § 507(a)(5) (1994).
  \item[87] In bankruptcy cases, fairness means equality of distribution among creditors similarly situated. See supra note 84 and accompanying text. This norm is imposed to encourage out-of-court workouts through cooperation and to discourage predatory or preferential activities, but it is also imposed because it is fair to treat entities with similar legal rights equally. This objective notion of fairness might not be acceptable to all scholars. For example, law-and-economics scholars have developed the norm of "superfairness" in which no class regards its share as less valuable than the shares received by other classes. See generally William J. Baumol, Superfairness: Applications and Theory (1986). Bankruptcy law does not cotton to subjective notions of fairness, except insofar as it favors a consensual plan of reorganization over a cramdown (nonconsensual) plan. See Richard F. Broude, Cramdown and Chapter 11 of the Bankruptcy Code: The Settlement Imperative, 39 Bus. L. 441, 454 (1984).
\end{enumerate}
\end{footnotesize}
markets lead to forfeitures and windfalls occasioned by laws that are skewed to advantage the swift, rapacious creditor at the expense of other creditors, the debtor, and society.\textsuperscript{88} Thus, we can begin to gauge the success of chapter 7 by comparing the relatively beneficial result in a chapter 7 liquidation case to the relatively costly result that we expect would be realized under nonbankruptcy law in the absence of chapter 7.\textsuperscript{89}

We should also measure success by the extent to which honesty and integrity pervade the system. Honesty and integrity are strong strange attractors in bankruptcy law. Not only must chapter 7 be efficient, it must not be corrupt. Regrettably, the opportunity to manage other people's money sometimes proves too tempting for some small portion of the private trustees charged with this responsibility.\textsuperscript{90}

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\textsuperscript{88} Commentators have recognized the efficiency gain that results from an orderly liquidation under chapter 7 of the Bankruptcy Code by comparison with the piecemeal forced sales that often eventuate under nonbankruptcy law. See Butler & Gilpatric, \textit{supra} note 13, at 279; Warren, \textit{Bankruptcy Policymaking}, \textit{supra} note 14, at 350. The policy of equality of distribution in bankruptcy cases operates to neutralize, in part, information asymmetries and the inequality of bargaining power that pervade the market. Creditors who obtain superior information by monitoring the debtor might act to obtain a judgment and levy on property under nonbankruptcy law before less vigilant creditors can act. Under some circumstances, bankruptcy law permits a trustee to avoid such a seizure as a preference. See 11 U.S.C. § 547 (1994). Any property recovered as a result of avoiding the preference will be for the benefit of the estate. See id. § 550(a). This equality principle encourages out-of-court negotiation and the sharing of information, which can optimize value in certain cases. Thus this policy is justifiable on the basis of efficiency as well as fairness.

\textsuperscript{89} It makes little sense to compare chapter 7 liquidation to a hypothetical perfect market when the reality is an imperfect market with information asymmetries and transaction costs. From a societal standpoint, the appropriate inquiry is comparing the net benefit (or cost) to society of liquidation under chapter 7 with the net benefit (or cost) to society that would result in the absence of chapter 7. See, \textit{e.g.}, \textit{infra} notes 96-101 and accompanying text.

\textsuperscript{90} See, \textit{e.g.}, \textit{In re} Foodsource, Inc., 130 B.R. 549 (N.D. Cal. 1991) (holding sureties liable for misappropriation of funds by trustee).
assets creates an allocative inefficiency; in addition, if the diversion is discovered, the entire bankruptcy system is faced with disrepute. A low level of corruption and the ability of parties and supervisors to ferret out corruption inexpensively and speedily are thus important components of a successful chapter 7 system.

Although one of the goals of chapter 7 is speedy administration, a system that sacrificed fairness for speed would be unsuccessful and unjust. The law addresses competing concerns of speed and due process by requiring the clerk's office to give creditors adequate notice and opportunity to participate in the distributive pool. Bankruptcy law prescribes an additional element of justice (or equity) that requires courts to decide the circumstances under which late-filed claims or administrative expenses should participate in the distribution.

b. A Speedy System.

A successful chapter 7 system should function smoothly without undue delay. But we cannot adopt a rigid standard to evaluate the pace of chapter 7 cases, because different facts and circumstances require different amounts of time and effort.

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91 See infra notes 94-101 and accompanying text.

92 See FED. R. BANKR. P. 2002(a). Speed in administration is a strange attractor in chapter 7, both in terms of the time value of money to creditors and in terms of the efficient use of judicial resources. See FED. R. BANKR. P. 1001 (requiring the Bankruptcy Rules to "be construed to secure the just, speedy, and inexpensive determination of every case and proceeding."). Due process of law is also a strange attractor in chapter 7, as it is in other areas of law. The public interest favors having the system operate fairly so that all creditors may have a reasonable opportunity to assert claims and be heard.

Nevertheless, the judge, clerk of court, and the Administrative Office might seek to evaluate chapter 7 cases based on government-determined norms to determine whether cases take too long to administer or return too little value to creditors.\textsuperscript{94} It is unjustifiable, however, to measure success solely from the perspective of public servants assigned to administer the system, when other players in the chapter system have independent perspectives with respect to these factors.\textsuperscript{95}

Instead, we should evaluate the success of the chapter 7 business liquidation case in light of the relative delay it imposes on secured creditors, landlords, and others with property interests that are subjected to the bankruptcy process. We should evaluate the delay to these parties in comparison with the delay they could expect to encounter in pursuit of their nonbankruptcy rights.\textsuperscript{96}

\textsuperscript{94} In nearly every district, more than 90\% of the chapter 7 cases result in no distributions to creditors, and most require little if any action by the assigned bankruptcy judge at any point. The median disposition time is an excellent indicator of how quickly the courts are processing these "routine" chapter 7 cases. See Ed Flynn, Explanation of the Statistical Tables and Graphs (1995) (unpublished memorandum from Bankruptcy Judges Division of Administrative Office of the United States Courts, on file with author). The accompanying table establishes that for 1994 the median disposition time for chapter 7 cases (including consumer cases) was 4.8 months, down from 5.1 months in 1993, and that only 3.1\% of the cases reach 2 years old. \textit{Id}. Therefore, we must inquire whether the disposition rates for chapter 7 cases are indicative of success. We should pose the same question with respect to distribution percentages. See \textit{supra} note 75.

\textsuperscript{95} The interests of those who are paid by the government to administer and adjudicate the bankruptcy system are fundamentally different from those who have a legal right to participate directly in the wealth generated by the estate. There is an undeniable feedback effect on the timely maximization of the value of the estate caused by the judges, clerks, trustees, and United States trustees who administer the system. To some extent the speed with which a case is processed depends on the government's allocation of scarce judicial and administrative resources. But we must also determine whether there are individuals in the system who desire to maximize their own position by doing the least amount of work for the greatest personal return.

\textsuperscript{96} It is insufficient to measure the absolute delay imposed on creditors by the
Thus, we should isolate those aspects of the chapter 7 process that account for incremental delay that would not be visited on creditors under nonbankruptcy law.

Even though chapter 7 partnership and corporate debtors do not receive discharges, they do obtain the benefits of the automatic stay.\(^{97}\) Debtors sometimes use "abusive" filings\(^{98}\) to obtain the benefit of the automatic stay in order to delay eviction\(^{99}\) or to prevent lien foreclosure.\(^{100}\) The cost of delay on pending civil litigation can be great as well. Consider the debtor who is sued and files chapter 7 on the eve of trial after a jury bankruptcy system. The more pertinent inquiry is to determine the delay imposed by the bankruptcy system relative to the delay which creditors would have suffered in pursuit of their rights under nonbankruptcy law.

The filing of a chapter 7 petition automatically stays the commencement or continuation of most suits against the debtor and acts to create, perfect, or enforce liens against property of the debtor or the estate. See 11 U.S.C. § 362 (1994). Thus both secured and unsecured creditors are delayed in their collection efforts by the filing of the chapter 7 petition.

Many commentators believe that the filing of a bankruptcy petition solely for purposes of delay is an abusive or bad-faith filing that warrants relief from the automatic stay or dismissal of the bankruptcy case. See Robert L. Ordin, The Good Faith Principle in the Bankruptcy Code: A Case Study, 38 Bus. L. 1795, 1808-11 (1983) (collecting cases). But abuse may be difficult to determine in the abstract. Some courts require both subjective bad faith and objective futility of any possible reorganization before dismissing a case as abusive. See Rolex Corp. v. Associated Materials, Inc. (In re Superior Siding & Window, Inc.), 14 F.3d 240, 242-43 (4th Cir. 1994). Although sequential filings can be indicative of abuse, changed circumstances can justify a subsequent filing even where a prior case has been dismissed for bad faith. Society Nat'l Bank v. Barrett (In re Barrett), 964 F.2d 588 (6th Cir. 1992).

Although courts are split over whether the automatic stay prevents eviction of a debtor that has no right to possess premises, the language of the statute appears to protect the debtor's possessory interest even if it is wrongful. See 11 U.S.C. § 362(a)(3) (1994). Compare, e.g., Cuffee v. Atlantic Business & Community Dev. Corp. (In re Atlantic Business & Community Corp.), 901 F.2d 325, 328 (3d Cir. 1990) (holding that stay prevents landlord from acting to terminate tenancy at sufferance) with, e.g., City Auto, Inc. v. Exxon Co., 806 F. Supp. 567 (E.D. Va. 1992) (holding that stay does not prevent eviction action). Of course, if the debtor is lawfully possessing premises, the automatic stay undoubtedly prevents the landlord from ousting the debtor or trustee from possession. See 48th St. Steakhouse, Inc. v. Rockefeller Group, Inc. (In re 48th St. Steakhouse, Inc.), 835 F.2d 427 (2d Cir. 1987), cert. denied, 485 U.S. 1035 (1988).

The automatic stay enjoins the foreclosure of liens against property of the estate
has been impaneled. If the trial is delayed, the parties, jurors, and the court system itself all incur costs. If the trial is canceled, the judge and others involved in litigation outside the bankruptcy court have wasted their entire investment in trial preparation.\footnote{101}

We need to determine these incremental costs and determine if they are offset by countervailing social benefits in the chapter 7 process. Although these costs are not easy to quantify, nonetheless they are costs of the system that we must consider.

c. An Inexpensive System.

Finally, to determine whether the chapter 7 system is relatively inexpensive, our definition of success must take account of hidden costs. The administrative expenses\footnote{102} attributed to the chapter 7 case do not begin to approximate the societal burden created by processing thousands of business bankruptcies through the federal court system each year.\footnote{103} In this day of limited resources, our definition of success

\footnote{101}{To be sure, if the trial is removed to the bankruptcy court or the issue is joined in the context of claims litigation, not all of the preparation on the part of the lawyers will be wasted. See FED. R. BANKR. P. 3007, 7052.}

\footnote{102}{Administrative expenses are described in § 503(b) of the Bankruptcy Code. 11 U.S.C. § 503(b) (1994). Court costs, taxes incurred by the estate, and professional fees are included within this category, \textit{id.}, which is entitled to first priority against the residual chapter 7 estate. 11 U.S.C. § 726(a)(1) (1994). The residual chapter 7 estate is comprised of the assets that remain after encumbered property of the estate or its proceeds is returned to secured creditors. See 11 U.S.C. § 725 (1994).}

\footnote{103}{Some commentators contend that the bankruptcy system is self-supporting as a result of user fees. \textit{See} Warren, \textit{Bankruptcy Policymaking}, \textit{supra} note 14, at 364-65. If this finding is correct, the degree to which the system internalizes its own costs should be one measure of its success. Of course, it is possible that certain users of the system are subsidizing others. If so, perhaps the cost of the latter type of case should be internalized through higher user fees as a percentage of assets when debtors have assets to pay such fees. We can speculate that if society as a whole benefits from the bankruptcy system, society should fund the shortfall that results when the assets of the particular case are insufficient to pay for its cost. Analysis of that proposition, however, is beyond the scope of this article.}
requires us to analyze whether the resources of a federal judge and support staff as well as the Office of United States Trustee (or estate administrator)\textsuperscript{104} are necessary or proper as part of the business liquidation process. Obviously the costs of bankruptcy are reflected not only in the salaries and benefits for the individuals who comprise the system, but in the hard costs for buildings, supplies, education, travel, and other factors used to support the system.\textsuperscript{105} A successful system might internalize its costs by being self-sufficient, not only in cases in the aggregate but on a case-by-case basis.\textsuperscript{106} Since the chapter 7 partnership or corporate debtor does not receive a discharge,\textsuperscript{107} perhaps Congress should require a minimum dollar amount of estimated assets as a jurisdictional threshold for businesses seeking to liquidate in federal court.\textsuperscript{108}

\textsuperscript{104} See supra note 73.
\textsuperscript{105} According to data prepared by the Administrative Office of the United States Courts, based on salaries effective January 1, 1995, each new bankruptcy judgeship costs an average of $735,530 for the first year and $614,631 per year thereafter. See H.R. Rep. No. 569, 104th Cong., 2d Sess. 4 (1996) & Memorandum from Judicial Impact Office, Administrative Office of the United States Courts (Feb. 16, 1996) (on file with author). Of this cost, $370,301 is for salary and benefits for the judge and supporting personnel. The balance is for expense and maintenance of the courts, space and facilities costs, court security, and an allocated share of costs incurred by the Administrative Office of United States Courts. Of course to some extent, the cost of existing facilities is a sunk cost. But presumably at least some of the facilities are assets that the government would reallocate if bankruptcy courts were down-sized or eliminated.
\textsuperscript{106} See supra note 103.
\textsuperscript{107} See supra note 52.
\textsuperscript{108} In the short run, the determination of a threshold should be based on the marginal cost of processing an additional case through the system, since certain fixed costs, such as maintaining the courthouse, are in place. In the long run, however, we should ask whether business liquidation cases should remain in the federal system, since the replacement of assets, such as judges and courthouses, might be driven by that determination. Although we should compare the cost to society that is incurred when a business is liquidated under the federal system to the cost avoided because the business is not liquidated under the state system, we should recognize that certain aspects of the state collection system must remain in place whether or not an alternative federal liquidation system is available. For example, creditors who obtain judgments against solvent debtors must have a mechanism
Nevertheless, because chapter 7 partnership and corporate debtors are destined to be liquidated, it is possible to harmonize the conflicting policy objectives of the various creditor and governmental interests in most chapter 7 cases. Our successful chapter 7 case is one that is relatively just, speedy, and inexpensive, and one that maximizes the value of the estate for monied parties in interest. Since competing interests have few available alternatives to chapter 7 and since chapter 7 provides relative efficiency gains, we might be able to approximate the success of chapter 7 simply by determining whether it maximizes economic value.

Although the complete theoretical definition of success would require fairness issues to be balanced with economic efficiency, there are few fairness issues that arise in business liquidation cases. In the voluntary chapter 7 case, the debtor's demise is certain, and creditors are treated in accordance with legislated priorities that generally recognize equality of distribution among creditors similarly situated. Thus, in this context, maximization of the economic value of the chapter 7 estate should correlate to enforce their judgments under state law whether or not an alternative federal system exists to regulate bankrupt debtors.

The absence of fresh-start considerations removes an additional layer of complexity from the policy analysis. In this context, the principal purpose of chapter 7 is to maximize the aggregate value of the debtor's assets for distribution to creditors using a collective approach that is grounded in equality of distribution for creditors with similar legal rights. When the debtor's fresh start is added as a strange attractor, the tension with the attractor of maximizing the value of the estate for distribution to creditors becomes obvious. If the debtor will receive a discharge, the debtor may have no incentive to maximize the return to unsecured creditors. Therefore the debtor may act to maximize its own position at the expense of creditors. For example, the individual debtor might seek to exempt property out of the estate even if its presence would enhance the value of other assets of the estate. See 11 U.S.C. § 522 (1994); FED. R. BANKR. P. 4003. This additional layer of complexity is absent in the chapter 7 liquidation case of the corporate or partnership business debtor. See also supra notes 59-62 and accompanying text.
highly with maximization of social value. Such is not the case, however, in the context of the business reorganization, where a partnership or corporate debtor will continue to operate a viable business and receive a discharge in a successful case.\footnote{110}

IV. **Defining Success In Chapter 11 Business Reorganization Cases.**

This part builds on the definition of success in chapter 7 to formulate a definition for chapter 11. It begins by describing the chapter 11 process, emphasizing differences between chapters 7 and 11. This part revisits the players and discusses their more complex goals and incentives in the reorganization context. This part concludes by developing a definition of success that moves beyond statistics-based measures to include broader measures that enable us to evaluate whether chapter 11 maximizes social enterprise value.

A. **The Basics of the Chapter 11 Process.**

Chapter 11 is designed to enable a business to reorganize when possible and to liquidate otherwise.\footnote{111} Generally\footnote{112} the case is commenced when the debtor files a voluntary petition with the bankruptcy court seeking relief under chapter 11.\footnote{113} The filing of the chapter 11 petition creates an estate that consists of all of the debtor’s interests in property.\footnote{114} The petition also invokes an automatic stay against creditors,

\footnote{110} In chapter 11 cases involving reorganization where the business continues, the Bankruptcy Code grants a pervasive discharge to partnership and corporate debtors. 11 U.S.C. § 1141(d) (1994). See infra text accompanying notes 136, 141.


\footnote{112} Creditors may commence a chapter 11 case against the debtor by filing an involuntary petition with the bankruptcy court. See 11 U.S.C. § 303 (1994).


thereby enjoining them from commencing or continuing most law suits against the
developer and from seeking to create, perfect, or enforce any lien against property of the
developer or of the estate.\textsuperscript{115} One purpose of the automatic stay is to give the debtor a
breathing spell in which it can seek to reorganize the business or its capital structure.

In most chapter 11 cases, the debtor remains in possession\textsuperscript{116} and can manage
its business in the ordinary course without obtaining a court order or creditor consent.\textsuperscript{117}
The United States trustee appoints a committee of creditors holding unsecured
claims\textsuperscript{118} to monitor the debtor’s business operations and negotiate a plan.\textsuperscript{119} The plan
may restructure the business\textsuperscript{120} or alter the debtor’s capital structure.\textsuperscript{121} Plan
negotiations are constrained by two financial fairness standards.\textsuperscript{122} First, dissenting
creditors must receive at least as much under the plan as they would receive in a
hypothetical liquidation of the debtor under chapter 7.\textsuperscript{123} Second, if a class of claims

\textsuperscript{116} When a trustee is not serving in the chapter 11 case, the debtor remains in possession. See 11 U.S.C. § 1101(1) (1994). The debtor in possession is given most of the rights and powers and responsibilities and duties of a trustee. See 11 U.S.C. §§ 1106(a), 1107(a) (1994).
\textsuperscript{118} Ordinarily, the United States trustee appoints creditors holding the seven largest unsecured claims if they are willing to serve. See 11 U.S.C. § 1102(a)(1) (1994).
\textsuperscript{120} The plan can restructure the business in many ways, such as by transferring or selling assets or by providing for the merger or consolidation of the debtor. See 11 U.S.C. § 1123(a)(5)(B)-(D) (1994).
\textsuperscript{121} The plan can alter the capital structure in many ways, such as by issuing new debt or equity securities or modifying or canceling existing obligations or liens. See 11 U.S.C. § 1123(a)(5)(E), (F), (J) (1994).
dissents, the plan must not discriminate unfairly against the class and must be fair and equitable with respect to the class. The requirement that a plan be fair and equitable with respect to a dissenting class roughly means that either the plan must provide for the class in full or no class that is subordinate to the dissenting class can receive or retain any property under the plan.

The Bankruptcy Code encourages negotiations to produce a consensual plan of reorganization. A consensual plan need not have unanimous support, because the law permits requisite majorities of creditors to vote to bind dissenters.

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126 See 11 U.S.C. § 1129(b)(2) (1994). See generally, Kenneth N. Klee, All You Ever Wanted to Know About Cram Down Under the New Bankruptcy Code, 53 AM. BANKR. L.J. 133 (1979). Courts have interpreted the fair and equitable requirement to impose an absolute priority rule whereby senior creditors must be compensated in full before junior creditors or owners can participate in distributions under the plan. See, e.g., Case v. Los Angeles Lumber Prods. Co., 308 U.S. 106, 117, 60 S. Ct. 1, 8 (1939). Sometimes the plan will distribute equity securities of the debtor to creditors holding unsecured claims. In order to determine whether the equity securities provide these creditors with value not less than 100% of their claims, the court must value the equity securities. Traditionally the court computes a value of the equity based in part on a capitalization of the future earnings of the reorganized debtor. Courts have recognized the imprecision of this enterprise valuation under the fair and equitable rule. See Consolidated Rock Prods. Co. v. Du Bois, 312 U.S. 510, 526, 61 S. Ct. 675, 685 (1941); Citibank, N.A. v. Baer, 651 F.2d 1341, 1347 (10th Cir. 1980). Commentators concur that this valuation process is uncertain. See, e.g., Chaim J. Fortgang & Thomas M. Mayer, Valuation in Bankruptcy, 32 UCLA L. REV. 1061, 1125, 1131 (1985); Isaac M. Pachulski, Cram Down and Valuation Under Chapter 11 of the Bankruptcy Code, 58 N.C. L. REV. 925, 943 n.84, 954-55 (1980).

127 See generally Broude, supra note 87.

128 The court determines acceptance of the plan by considering the votes of each class. The plan must group creditors' claims and ownership interests into classes. See 11 U.S.C. § 1123(a)(1) (1994). Only claims and interests that are substantially similar may be classified together. See id. § 1122(a). A class of claims votes to accept the plan when it receives the affirmative votes of at least
usually the proponent of the plan. The plan proponent must convince the court to confirm the plan at a confirmation hearing before the plan can be effective. To confirm a consensual plan, the court must find, *inter alia*, that it meets the requisite fairness standard and that confirmation "is not likely to be followed by the liquidation, or the need for further financial reorganization, of the debtor." 

A plan proponent may be able to persuade the court to confirm a plan over the dissent of one or more classes in certain limited circumstances. Once a plan is confirmed, if the debtor's business has been reorganized, the debtor receives a discharge of all debts that arose before the date of confirmation.

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130 The court must determine that the plan meets at least 13 confirmation requirements before the court enters its order confirming the plan. See 11 U.S.C. § 1129(a)(1)-(13) (1994).
131 Even if all parties support the plan, the Bankruptcy Code requires the court to hold a confirmation hearing. See 11 U.S.C. § 1128(a) (1994).
132 The plan usually specifies an effective date on which it will become operative. Unless the plan or the order confirming the plan otherwise provides, confirmation of the plan binds all parties whether or not they have voted for the plan. See 11 U.S.C. § 1141(a) (1994).
133 In the context of a consensual plan, the requisite fairness standard protects dissenting creditors from receiving less under the plan than they would have received in a hypothetical liquidation of the debtor under chapter 7. See 11 U.S.C. § 1129(a)(7)(A)(ii) (1994).
136 Chapter 11 of the Bankruptcy Code affords the opportunity for a fresh start to reorganizing businesses, including partnerships and corporations. See 11 U.S.C. § 1141(d) (1994). The reorganized business is freed of unsecured debts except as provided in the plan of reorganization, *id.*; the bankruptcy judge is supposed to determine that the reorganized business has a reasonable likelihood of repaying the debt obligations under the reorganization plan. See 11 U.S.C. § 1129(a)(11) (1994). Thus the reorganized business is given an opportunity to be a productive
The chapter 11 plan process involves negotiations that are influenced by uncertain future values and events and are conducted among parties who have less than perfect information. The parties cannot be certain of the viability of the business, its future earnings and cash flows, or its cost of debt or equity capital. During plan negotiations, the information on which the parties base their negotiating positions almost certainly will change. Yet the possible results of negotiations are restricted by economic factors. Thus the chapter 11 process is dynamic, turbulent, and unpredictable, but bounded in possible results; in short, it is chaotic. With this basic understanding of the chapter 11 process, we can explore the parties’ goals and incentives.

B. The Players And Their Complex Goals And Incentives.


A chapter 11 business reorganization is much more complex than a chapter 7 business liquidation case. This complexity is caused by conflicting goals among the creditor constituencies and between creditors and the debtor with respect to the debtor’s fresh start. Other causes of complexity include uncertainty respecting the viability of the debtor’s business and the value of the reorganized business.

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element of society once again in much the same way as the honest individual debtor under chapter 7. See supra note 59 and accompanying text. But unlike the individual debtor, the reorganized partnership or corporation cannot exempt property from the reach of creditors who hold debts under the plan. See 11 U.S.C. § 522(b) (1994). In the event of a postconfirmation default, creditors may obtain judgments under nonbankruptcy laws to enforce their judgments against the reorganized debtor’s property.

See generally MacDonald et al., supra note 14.

Although not all chapter 11 reorganization cases are complex, the typical reorganization case involving a business will have one or more secured creditors; unsecured creditors entitled to different priorities, such as employees and taxing agencies; general unsecured creditors; and shareholders. Large chapter 11
2. The Debtor.

The incentives for the business debtor in chapter 11 differ significantly from those of a debtor in chapter 7.

a. The Debtor’s Survival.

In reality, the debtor may or may not seek to maximize the value of the business enterprise, because the debtor primarily is interested in survival and its fresh start. If a risky strategy is necessary for survival, the debtor might pursue it even if the expected value is less than the value we would expect from a more conservative strategy. In many cases the expected values of different strategies will be unclear, and the debtor may have the relative advantage of an information asymmetry in making its business decision. The debtor’s pursuit of a risky strategy might be inefficient, ex post, and also may violate the debtor’s fiduciary duty of care to creditors. But the debtor’s survival impetus is a strong strange attractor in the chapter 11 process.

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139 Outside bankruptcy the debtor has a has a fiduciary duty of care to shareholders when the debtor is solvent. When the debtor is in the vicinity of insolvency, the duty shifts to creditors and shareholders. In bankruptcy, if the debtor is insolvent, it appears that the debtor in possession (or trustee) has a duty of care to creditors first and shareholders second. See, e.g., CFTC v. Weintraub, 471 U.S. 343, 105 S. Ct. 1986 (1985).
b. The Debtor's Fresh Start.

Public policy strongly favors the debtor's fresh start to preserve jobs and avoid the costs of liquidation, when the debtor's survival will maximize value. Specifically, the ability of a corporation or partnership to receive a discharge in a chapter 11 case often is critical to the entity's ability to reorganize. In this sense, the purpose of chapter 11 reorganization is to reorganize the business, management, and capital structure as necessary to maximize value, while at the same time avoiding the transaction costs and societal costs that would otherwise be occasioned by liquidation of the business. The debtor's discharge is a strange attractor in chapter 11, as are avoidance of transaction costs and societal costs.

c. Management's Incentives.

In addition, we can identify a potential employment-incentive and agency problem that is absent in chapter 7. Often individual managers of the debtor are

140 See supra note 7. The concept of fresh start for the chapter 11 business debtor is related to but different from the fresh start given to the individual debtor in a chapter 7 liquidation case. See supra notes 59, 109, 136. The individual debtor must continue to survive and consume resources, whereas the business debtor may be liquidated and dissolved. But just as the individual debtor is entitled to discharge debts to facilitate a fresh start, the business debtor must receive a discharge if it is to have a reasonable opportunity to survive. Thus if survival of the business enterprise is the means to maximize value, the discharge will facilitate survival.

141 Unless the plan or the order confirming the plan otherwise provides, confirmation of the plan generally discharges the corporate or partnership debtor from all debts that arose prior to confirmation. 11 U.S.C. § 1141(d)(1) (1994). The discharge precludes a creditor from seeking legal enforcement of the discharged debts against the debtor. See 11 U.S.C. § 524(a) (1994).

142 Another way to view the problem is to consider the value of external relationships as part of the going concern bonus that should be maximized from a societal standpoint. See Butler & Gilpatric, supra note 13, at 280-83. In this respect, the problem of business rehabilitation must be seen "not merely [as] a crisis of dollars, but [as] a crisis of values experienced in individual ways by those who have contributed to and are affected by the enterprise." Korobkin, Rehabilitating Values, supra note 28, at 766.
concerned about preserving their jobs. To the extent they do not have ownership interests in the debtor, this may create a conflict between maximizing value for owners and preserving jobs for managers. On the other hand, to the extent the managers have ownership interests in the debtor, if the debtor becomes insolvent, they may be willing to gamble with assets that otherwise would be distributed to senior creditors in order to generate value for their junior interests. For these reasons, among others, managers of businesses in chapter 11 cases are biased against liquidation.


Secured creditors often seek to maximize value, but not necessarily the value of the estate. Secured creditors generally are interested in maximizing the recovery from their collateral and the recovery on any deficiency claim. One method by which a

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143 Indeed, some commentators contend, without supporting data, that managers whose companies file chapter 11 reorganization cases often retain their jobs. See Lawrence H. Kallen, Corporate Welfare: The Megabankruptcies of the 80s and 90s, at 468 (1991). But see LoPucki & Whitford, Patterns, supra note 12, at 610 (finding otherwise in a study of publicly-held companies that filed reorganization cases under chapter 11). Some commentators believe that management’s ability to consume private benefits in chapter 11 cases causes a restriction on the debtor’s availability of credit ex ante, with a result that the debtor underinvests outside of bankruptcy. See Alan Schwartz, Contracting About Bankruptcy 6 (Feb. 1996) (unpublished manuscript, on file with author).

144 This incentive for managers to gamble inefficiently would disappear (in theory) if the managers owned interests proportionate to the various debt and equity interests in the case after giving effect to their ability to consume private benefits.

145 A secured creditor holds a lien that encumbers property of the estate. See 11 U.S.C. §§ 101(10), (37) & 506(a) (1994). A creditor is undersecured when the value of its collateral is less than the amount of its allowed claim against the estate. In chapter 7 or chapter 11, an undersecured creditor with recourse against the debtor holds an allowed secured claim equal to its interest in the collateral and an unsecured deficiency claim for the amount by which the creditor’s allowed claim exceeds the value of the collateral. See 11 U.S.C. §§ 501, 502, 506(a), 1111(a) (1994). In chapter 7, if the creditor holds a nonrecourse claim, its claim for deficiency will be subject to disallowance, because the creditor could not assert the claim against the debtor under nonbankruptcy law. See 11 U.S.C. §§ 102(2), 502(b)(1) (1994). In chapter 11, however, in some circumstances the nonrecourse creditor is given an unsecured deficiency claim even though one
secured creditor might maximize the recovery on its collateral is to extract the collateral from the estate and pursue state law remedies against the collateral. Where the creditor is undersecured to a significant extent, however, the creditor might prefer an "investment" of the collateral in a rehabilitated business enterprise in order to increase recovery on the creditor's unsecured deficiency claim. To the extent the creditor's unsecured deficiency claim is dominant, the creditor could have interests similar to the unsecured creditors.\footnote{146} Typically, however, the secured creditor is a lending institution that does not have the same incentives as trade creditors, who may wish to provide goods or services to the debtor going forward. Moreover, inefficient regulatory criteria might pressure the lender to make suboptimal economic decisions.\footnote{147} Thus, secured creditors are less likely than unsecured creditors to be tolerant of delay in the reorganization process, particularly if their collateral positions are eroding.

\footnote{146} The partially secured creditor may hold collateral that is worth little when compared to the entire debt. If so, the unsecured claim may be the predominant source of recovery for the creditor. In that event, the partially secured creditor's interests may be closely aligned with those of the unsecured creditors.

\footnote{147} Regulated financial institutions may be subject to regulations that preclude them from holding voting equity securities of nonbanks. See 12 U.S.C. § 1843(a) (1994). Moreover, before 1993, FASB Statement No. 15 generally permitted financial institutions to avoid writing down of restructured loans if the undiscounted future cash flows were not less than the recorded investments in the loans before restructuring. See FASB Statement No. 15 (1992). Between 1993 and 1994, the accounting standards changed to require financial institutions to consider the present value of future cash flows of loans involved in troubled debt restructurings. See FASB Statement No. 114, Accounting by Creditors for Impairment of a Loan, as amended by FASB Statement No. 118, Accounting by Creditors for Impairment of a Loan-Income Recognition (1994). The former standards might have influenced financial institutions to make decisions that were inefficient. While the financial institution might have been acting to maximize its own position, its actions probably left society worse off by causing the debtor to be overleveraged. The new standards should eliminate this disfunction.
Finally, secured creditors are likely to be players in more than one chapter 11 case. A secured creditor might act in a manner that is suboptimal in a specific case in order to maximize value in other cases. Thus the goals of a particular secured creditor in a given case may be difficult to predict. This information asymmetry creates a turbulence that makes traditional economic measures of success suspect and suggests that we should apply chaos theory instead.

4. Unsecured Creditors.

While unsecured creditors have the same goal as in chapter 7, maximizing the value of the estate, the method of maximization varies. In some cases, reorganization of the business enterprise as a going concern, which may or may not require a change of management, will maximize value. In other cases, liquidating the business

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148 See infra text accompanying note 159.
149 See supra note 7.
150 Continuation of management must be consistent with the interests of creditors and equity security holders and with public policy. 11 U.S.C. §§ 1123(a)(7), 1129(a)(5)(A)(ii) (1994). Although management continues to operate the reorganized business in many small cases, in larger cases it is common for management to change during the reorganization process. See LoPucki & Whitford, Patterns, supra note 12, at 610-11; LoPucki & Whitford, Corporate Governance, supra note 56, at 723-26 (finding a change in chief executive officer in 70% of the cases in contemplation of or during a chapter 11 case). In either event, the business may be reorganized successfully. For example, in the Revco D.S., Inc. case, a failing drugstore chain was successfully recapitalized under new management, producing a result far superior to liquidation. See Disclosure Statement at 17, in re Revco D.S., Inc., 131 B.R. 615 (Bankr. N.D. Ohio 1990) (case nos. 588-1308 et al) ("In connection with a series of senior management changes, the persons who had served as [the senior management] . . . resigned in late 1987" and were replaced by new management who filed a chapter 11 petition for Revco on July 28, 1988). In the Hillsborough Holdings Co. case, a diverse group of companies was reorganized under their former management team, likewise producing a result far superior to liquidation; creditors, however, gained the right to designate a majority of the board of directors. See Supplement to Disclosure Statement at 27-29, in re Hillsborough Holdings Corp., 187 B.R. 763 (Bankr. M.D. Fla. 1995).
in an orderly fashion will produce better results for unsecured creditors. In rare circumstances, the business liquidation requires immediate cessation of operations and a rapid liquidation sale. In order for creditors to determine which remedy is necessary to maximize value, they must be able to obtain and analyze business information. Therefore, while unsecured creditors usually do not favor delay, they require a certain amount of delay in order for them to obtain and process information to make rational decisions.

151 Where the core business of a company is losing money on an operating basis, its value as a going concern is negative. That is, continued operations will consume assets even if the company is debt-free. In these circumstances, prompt liquidation of the company is often better for society as well as for the company’s creditors. See, e.g., Robert K. Rasmussen, The Efficiency of Chapter 11, 8 BANKR. DEV. J. 319, 320-21 (1991) (criticizing bankruptcy judge for allowing Eastern Airlines, Inc. to dissipate $600 million in an effort to save the business). LoPucki and Whitford contend that most large, publicly held companies “liquidate some assets and a few liquidate all assets.” LoPucki & Whitford, Patterns, supra note 12, at 605.

152 For example, where continued operations would create pollution in violation of environmental laws, often society and creditors would prefer that the business be shut down and liquidated. See, e.g., United States v. LTV Corp. (In re Chateaugay Corp.), 944 F.2d 997, 1008 (2d Cir. 1991) (finding cleanup order relating to ongoing pollution nondischargeable); Alabama Surface Mining Comm’n v. N.P. Mining Co. (In re N.P. Mining Co.), 963 F.2d 1449, 1461 (11th Cir. 1992) (granting administrative expense priority to postpetition environmental fines). Liquidation not only prevents additional pollution by the debtor but may provide funds to clean up existing pollution. Cf. Midlantic Nat’l Bank v. New Jersey Dep’t of Envtl. Protection, 474 U.S. 494, 106 S. Ct. 755 (1986) (refusing to allow trustee to abandon polluted property).

153 The debtor is required to file certain financial information, unless the court orders otherwise. 11 U.S.C. § 521(1) (1994). Typically, the United States trustee will require the debtor in possession to file additional operating reports and interim statements that disclose data respecting the ongoing operation of the business. And creditors or an active creditors’ committee can adduce additional financial information from the debtor on a voluntary basis or through discovery. See FED. R. BANKR. P. 2004, 7026-7037; Kenneth N. Klee & K. John Shaffer, Creditors’ Committees Under Chapter 11 of the Bankruptcy Code, 44 S.C. L. REV. 995, 1047-48 (1993).

154 See Klee & Shaffer, supra note 153, at 1047-48. In the ordinary chapter 11 case, creditors usually analyze financial information respecting the debtor before deciding whether to seek to convert the case to chapter 7 liquidation, dismiss the case, negotiate with the debtor over a consensual plan, or seek to file a creditors’
In addition to the maximization goal, certain unsecured creditors may have an additional goal to continue to deal with the debtor. For example, suppliers may value future business dealings with the debtor more than their claims against the debtor. Other creditors who intend to have no future dealings with the debtor will not share this additional goal. Sometimes maximization of a supplier's position will put these goals in conflict; it might be necessary for the supplier to sacrifice a short-term return on the supplier's claim against the debtor in order to aid recapitalization efforts that will lead to profitable future trade.

Of course it is possible that some unsecured creditors might not desire to maximize the value of the business, because they would be better off if the debtor failed to reorganize. Repeat players in bankruptcy cases might sacrifice a position in one case to maximize value elsewhere. For example, a labor union might take a suboptimal position on behalf of workers in a given case in order to uphold national bargaining positions that could affect workers in other businesses. Moreover, a creditor which is also a competitor of the debtor might profit if the debtor's business liquidates, even if the return on the competitor's claim in the case is suboptimal. Thus, as is the case for secured creditors, unsecured creditors may have conflicting goals that are difficult to determine. The resulting turbulence compounds the difficulty of applying a traditional economic calculus. The problem raised by these competing goals calls out for

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plan. See 11 U.S.C. §§ 1112(b), 1121(c) (1994). Creditors will need less time to acquire information in a prepackaged or prenegotiated chapter 11 case, in which a great deal of negotiation and information exchange takes place before the chapter 11 case is filed. See infra note 168 and accompanying text.
application of chaos theory to identify the patterns involved and a balancing test to reconcile competing economic and fairness concerns.

5. Other Constituencies.

In addition to unsecured creditors, secured creditors, and the debtor, there are many other constituencies in the chapter 11 process pursuing objectives that could affect the success equation. Employees of the debtor wish to retain their jobs. Owners of the debtor wish to maximize the value of their interests. Governmental agencies that deal with the debtor wish to make sure that the debtor conforms to laws, rules, and regulations and contributes revenue to the government as though the debtor were not in bankruptcy. Lawyers, accountants, investment bankers, and turn-around consultants who render services in chapter 11 cases generally prefer reasonably complex, non-litigious chapter 11 cases that result in confirmed plans and success fees or enhancements based on results. On the other hand, it is the author's experience

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155 In theory we could include the employees of the bankruptcy system as a constituency. Those who administer the bankruptcy system, such as judges and clerks, enjoy the extra "weight" they receive for chapter 11 cases, but prefer that the cases proceed expeditiously, without a lot of paper and pleadings, and that they result in confirmed plans and closed cases within a reasonable time. We should accord these preferences little or no weight in determining what is optimal for society. Rather, we must evaluate the use of judicial resources as a cost of the system in producing beneficial results.

156 Butler and Gilpatric recognize the importance of the debtor's relationships with employees, contracting parties, and parties with whom the debtor deals without a formal contractual relationship. See Butler & Gilpatric, supra note 13, at 282-83.

157 The Supreme Court has recognized the debtor's employees as a constituency whose interests must be considered. See NLRB v. Bildisco & Bildisco, 465 U.S. 513, 527, 104 S. Ct. 1188, 1196 (1984) ("Determining what would constitute a successful rehabilitation involves balancing the interests of the affected parties—the debtor, creditors, and employees.").

that certain lenders prefer contentious chapter 11 cases to "send a message" to their nonbankrupt borrowers that the institution is "tough."  

C. Measuring Success In Chapter 11.

This section defines success in chapter 11 by starting with economics and considering statistics-based measures. It then moves beyond economics to consider maximization of social enterprise value. The section next compares chapter 11 with alternatives and studies the indirect costs of liquidation on society. After discussing the exclusion of certain cases from eligibility for chapter 11, this section concludes by analyzing which data are important to determine the success of chapter 11.

1. Beyond Economics.

Based on this brief analysis of some of the various goals and policies that may be present in chapter 11 business reorganization cases, it is not surprising that the definition of success will vary based on the identity and viewpoint of the person or institution being asked to define it. Nevertheless, we must decide whether success can be limited to the perspective of the debtor and creditors in the reorganization case. Some commentators define success as the maximization of value for the various monied interests in the chapter 11 case.  

By necessity, this approach focuses on

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159 It is also possible that certain expert witnesses and litigators prefer contentious chapter 11 cases that have sufficient assets to pay their fees. But expert witnesses and litigators with a sufficient supply of work may prefer less contentious cases or settlements.

efficiency and ignores broader questions about whether the chapter 11 system is fair and just.\footnote{161}

While it is certainly not meaningless to define success from the limited perspective of each particular economic component that comprises the bankruptcy system, from a societal standpoint it is far more beneficial to define success in global terms by measuring the outcomes in the universe of chapter 11 cases against economic and social norms.\footnote{162} Specifically, from a societal standpoint, why does chapter 11 exist, what is its objective, and how can we measure whether the objective has been accomplished in a particular case and across a universe of cases?


In the opinion of this author, chapter 11 exists to maximize social value by providing a mechanism that is just, speedy, inexpensive,\footnote{163} and designed to maximize

\footnote{161} Dean Robert Scott notes that law-and-economics analysts "simply have chosen to ignore distributional concerns, because their tools have nothing useful to say about the picture." Scott, supra note 32, at 344.

\footnote{162} See Korobkin, Rehabilitating Values, supra note 28, at 772 ("The estate is not merely an economic pie to be deployed and distributed. It is a medium by which the enterprise's moral, political, social, and economic aims are defined and redefined."). Other commentators agree with this broad definition, but approach the problem from an efficiency perspective. See Butler & Gilpatrick, supra note 13, at 269 ("[M]any goals usually argued to be redistributive in nature are better understood as efficiency concerns."). Thus some economists will attempt to quantify moral, political, and social aims as part of a utilitarian efficiency analysis. Since different people value moral, political, and social issues differently, these economists must explicitly weigh preferences of different people or treat all people identically. Because cultural differences abound and values change over time, rather than jamming the moral, political, and social "Yin" values into the "Yang" world of quantifiable economics, this article opts for an unquantifiable evaluation of the collective moral, political, and social components of social enterprise value. As developed more fully in the Appendix, all of these factors comprise a Gestalt.

\footnote{163} We have already seen the virtues of a just, speedy, and inexpensive system in the chapter 7 context. Similar concerns apply to the chapter 11 context that justify our incorporation of these elements in a definition of success for chapter 11. See supra notes 80-110 and accompanying text.
the economic value of the debtor, while accommodating unquantifiable social values. This article uses the term "social enterprise value" to reflect the net social and economic benefit to society when a debtor is reorganized. Similarly, "social liquidation value" is the net social and economic value to society when a debtor is liquidated (or reorganized outside chapter 11). We should evaluate the success of chapter 11 by determining the extent to which it reorganizes debtors that should be reorganized and liquidates (or reorganizes outside chapter 11) those business that should be liquidated.

As more fully set forth in the Appendix, part of social enterprise value is quantifiable: the economic value of the enterprise (net of quantifiable externalities and spill-over effects), plus the avoided costs of liquidation (or other reorganization alternatives), less the avoided benefits of liquidation (or other reorganization alternatives). Social enterprise value also requires consideration of unquantifiable, noneconomic values attendant to reorganization, liquidation, or other alternatives. This consideration requires us to examine the moral, political, and social aspects of social enterprise value.\textsuperscript{164} By definition, as more fully developed in the Appendix, maximization of social enterprise value will be accomplished when the debtor reorganizes under chapter 11 as a synergistic going concern,\textsuperscript{165} unless liquidation or

\textsuperscript{164} Korobkin agrees that chapter 11 "is best understood as creating conditions for the realization of both economic and noneconomic aspects of the personality of the financially distressed corporation." Korobkin, \textit{Rehabilitating Values}, supra note 28, at 755. In forming a value-based account of bankruptcy law, Korobkin characterizes bankruptcy law as "a response to the problem of financial distress—not only as an economic, but as a moral, political, personal, and social problem that affects its participants." \textit{Id.} at 762.

\textsuperscript{165} See Cross Elec. Co. v. United States, 11 B.R. 998, 1000 (W.D. Va. 1980) ("There is a strong public policy which favors rehabilitation of failing concerns to make them viable contributors to society once again, rather than liquidating the companies quickly to turn over a reduced sum to all creditors."), \textit{rev'd on other grounds}, 664 F.2d 1218 (4th Cir. 1981).
other financial reorganization of the business would yield a higher net social enterprise value.\textsuperscript{166}

The moral, political, and social aspects of chapter 11 put its economic efficiency in context. For example, economic value for the business and its creditors might be optimized if the debtor were reorganized to permit it to utilize indentured servants to produce its goods. While the result might produce economic success, it would be a social failure because it violates basic precepts of human decency (not to mention the 13th Amendment).\textsuperscript{167} Our definition of success must recognize that the reorganized business is a component of society that both affects and is affected by quantifiable and unquantifiable externalities and transaction costs. Even if the quantifiable aspects of social enterprise value indicate that liquidation is preferable to reorganization, unquantifiable factors such as justice, flexibility, and adaptability might point to the opposite conclusion. Human judgment must be used to reconcile these competing conclusions.

\textsuperscript{166} In certain cases, the business will have a greater liquidation value than going concern value. If so, the Bankruptcy Code precludes the court from confirming a reorganization plan, for two reasons. First, dissenting creditors must receive at least as much as they would in a hypothetical chapter 7 liquidation of the debtor. See 11 U.S.C. § 1129(a)(7)(A)(ii) (1994). Second, dissenting classes are protected by the fair and equitable standard, which requires the court to value the enterprise at the greater of liquidation value or reorganization value. See, e.g., 11 U.S.C. § 1129(b)(1) (1994); \textit{In re} Puerto Rican Am. Tobacco Co., 112 F.2d 655, 656-57 (2d Cir. 1940). In these cases, unless creditors unanimously consent to a reorganization plan, the only confirmable plan will provide for liquidation or split up of the debtor’s assets.

\textsuperscript{167} U.S. CONST. amend. XIII. An economic efficiency or utility analysis would compare the value generated under a free system with a slave system by quantifying the costs of slavery. It is possible that a majority (absolute or weighted) would prefer a slave system even though a minority would not; nevertheless, some of our laws protect the rights of a minority, even when it is inefficient to do so.
Some academics have challenged the wisdom of any theory of chapter 11 that ventures beyond maximizing the economic value of the enterprise.\textsuperscript{168} Certain of these academics suffer from the linear thinking that accommodates their belief in the fantasy of a free market in which perfect information enables an optimal reallocation of resources in frictionless transactions.\textsuperscript{169} In fact, the lack of perfect information that pervades commerce leads to suboptimal transactions that are best evaluated under a chaotic model; such a model would incorporate positive feedback occasioned by political, psychological, and other unquantifiable components and recognize the significant transaction costs in economic and societal terms that accompany a liquidation.\textsuperscript{170}


\textsuperscript{170} See MacDonald et al., \textit{supra} note 14, at 28-31 (describing the chaotic nature of bankruptcy in a scientific sense); Korobkin, \textit{Rehabilitating Values, supra} note 28, at 773 (describing the chaotic nature of bankruptcy from an unscientific perspective). Korobkin notes that "[t]he chaos of financial distress is the chaos created when the participants make . . . difficult choices at cross-purposes, without any larger perspective as to their effects on the enterprise." \textit{Id.} at 773.

Professor Duncan Kennedy has discussed the chaotic positive feedback effect in a different context; specifically, he analyzes the consequential effects of wealth changes resulting from an efficiency analysis that is predicated on costless bargaining:

If we proceed to modify entitlements to replicate the outcomes of costless bargaining, letting the distributive consequences fall where they may (or modifying them ad hoc to correspond to some set of ethical preferences), then we are likely eventually to bring about wealth changes large enough to call in question everything we have done before.

Kennedy, \textit{supra} note 33, at 436.
a. Transaction Costs.

In order for us to determine whether chapter 11 produces optimal social enterprise values, we must examine transaction costs. In analyzing the relative value of chapter 11 and its alternatives, we must consider transaction costs imposed by chapter 11, including delay in distribution to creditors and incurrence of administrative expenses.\textsuperscript{171} We must also consider whether chapter 11 avoids transaction costs that would be incurred outside of chapter 11, such as preservation of capital and labor resources and reinforcement of societal moral values.\textsuperscript{172}

\textsuperscript{171} Ronald Coase viewed the firm as an enterprise that reduces transaction costs by bringing together collective resources that can substitute coordinated activity for the negotiation of separate transactions. Ronald H. Coase, The Nature of the Firm, 4 ECONOMICA (n.s.) 391-93 (1937). See also Butler & Gilpatric, supra note 13, at 280 ("Of course this coordination carries costs of its own, such as the administrative costs of managing the firm. A firm will exist if it can successfully coordinate the production of a good with lower transaction costs than are possible using market exchanges."). Considerable costs are incurred in administering a chapter 11 case. See 11 U.S.C. § 503 (1994) (listing categories of expenses). The estate bears the cost of fees and expenses incurred by professionals employed by the debtor in possession or the creditors' committee. See id. § 503(b)(2). These fees and costs can consume a large portion of small estates and about 3% of larger estates. See infra notes 190-191.

Our assessment of the costs of chapter 11 cannot be determined by size alone. Rather, we must recognize that chapter 11 is not monolithic; certain cases are filed only after negotiations or votes occur out of court. Cf. 11 U.S.C. § 1126(b) (1994) (prescribing conditions under which votes cast before the filing of the chapter 11 petition may be used to confirm a plan). These cases are called "prenegotiated" or "repackaged" cases. The costs may be less for a prepackaged or prenegotiated chapter 11 case than for an ordinary chapter 11 case. See Elizabeth Tashjian et al., Prepacks: An Empirical Analysis of Prepackaged Bankruptcies, 40 J. Fin. ECON. 135, 143-47 (1996).

\textsuperscript{172} Although it is not intuitively obvious, one of the reasons for the success of chapter 11 is that it avoids transaction costs imposed in the cut-of-court workout or liquidation contexts. For example, Professor Gilson has identified at least five instances in which transaction costs for chapter 11 companies may be less than for companies that restructure out of court. See Stuart C. Gilson, Transactions Costs and Capital Structure Choice: Evidence from Financially Distressed Firms 3 (1995) (unpublished manuscript, on file with author). Specifically, Gilson notes that chapter 11 causes lenders to write down loans, provides tax advantages for cancellation of debt, binds dissenting creditors, mandates disclosure of
b. Synergy And Externalities.

In order to evaluate whether chapter 11 is successful, we must examine those cases in which the process has tended to maximize social and economic enterprise value to produce a result in excess of the net value that would be produced by pursuit of alternatives to chapter 11.\textsuperscript{173} Economic enterprise value can exceed liquidation value because of synergy, because the whole is greater than the sum of its parts, or because the owner of the assets has a particular ability to maximize economic value that another owner (or lender) lacks. From a societal viewpoint, social enterprise value may exceed social liquidation value because of the value of external relationships between the debtor and its employees, retirees, customers, and suppliers.\textsuperscript{174} The avoidance of liquidation costs, such as severance and unemployment benefits, welfare, and retraining costs, can also create a social enterprise value in excess of liquidation value.

c. Flexibility And Adaptability.

One of the principal benefits to society of the chapter 11 system is its encouragement of flexibility and adaptability by business managers.\textsuperscript{175} Just as the

\textsuperscript{173} The Supreme Court has recognized that lower courts must consider the consequences of the primary alternative of liquidation in deciding whether to take steps within the chapter 11 case to facilitate reorganization. See NLRB v. Bildisco & Bildisco, 465 U.S. 513, 527, 104 S. Ct. 1188, 1196 (1984); United States v. Whiting Pools, Inc., 462 U.S. 198, 203, 103 S. Ct. 2309, 2312-13 (1983).

\textsuperscript{174} See Butler & Gilpatric, supra note 13, at 281.

\textsuperscript{175} See infra note 182 and accompanying text.
pursuit of state court remedies or the imposition of personal liability on managers and owners can destroy innovation and risk-taking, the presence of the chapter 11 system can encourage them. Measuring this aspect of success of the chapter 11 business reorganization process may be difficult, if not impossible. But that it cannot be measured does not mean that it does not exist.

3. A Comparative Analysis.

This statement of success is only a first step. The analysis of alternatives to chapter 11 is not straight-forward.

a. Liquidation Alternatives.

We begin by considering those cases in which the principal alternative is liquidation of the business. It is not inevitable that in the absence of a chapter 11 reorganization case, a business would have to liquidate under chapter 7. If the business must terminate, it might meet its demise through a general assignment for the benefit of creditors, through an out-of-court liquidation, or through piecemeal decimation by the exercise of creditor remedies, including foreclosure, eviction, levy, peaceful repossesion, and the like.

A complete analysis of the success of liquidation alternatives to chapter 11 would properly consider the transaction costs of liquidation, including direct and indirect costs.

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176 But see Schwartz, supra note 143, at 6 (arguing that the debtor's or management's ability to consume private benefits in bankruptcy causes a contraction in credit and underinvestment).

177 See Tribe, supra note 35, at 1361-62.

178 A debtor makes a general assignment for the benefit of creditors by conveying all of the debtor's assets to an assignee; the assignee liquidates the assets and makes a distribution to creditors, with any surplus returning to the debtor. See supra note 54.
Direct costs of liquidation would include fees and costs of liquidation intermediaries, necessary advertising required by state law, and any costs of assembling, transporting, and disposing the debtor's property. Indirect costs would include the inefficiencies of state remedies such as sheriff's sales and foreclosure sales, as well as the costs of social benefits extended to those who become unemployed or are in need of retraining. Further indirect costs might arise from health problems caused by the trauma of liquidation.

From a broader perspective, the utilization of state-court remedies to liquidate the business can have a greater negative societal effect than is properly attributable to any particular case. Significantly, the inability of debtors to preserve businesses through reorganization can result in the destruction of innovation and risk-taking because of the inherent inequality of bargaining power that exists between most lenders and debtors. Stated differently, without a reorganization alternative, certain business managers might be less prone to take risks and develop new products. At the margin, potentially viable businesses will liquidate.

For example, in England, where directors of insolvent corporations have personal liability to creditors, directors are prone to liquidate businesses rather than risk

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179 | Auctioneers, liquidators, advertisers, and brokers are among the different kinds of liquidation intermediaries.

180 | Some commentators have recognized that reorganization under chapter 11 avoids certain of these indirect costs. See Donald R. Korobkin, Value and Rationality in Bankruptcy Decisionmaking, 33 WM. & MARY L. REV. 333, 354 (1992).

181 | Health problems and traumas also occur in some chapter 11 cases. See SOL STEIN, A FEAST FOR LAWYERS INSIDE CHAPTER 11: AN EXPOSE 36 (1989) ("Several months after filing every executive in our firm was sick . . . .").

182 | Of course, we should not encourage all risk-taking activities. Investment decisions should be based on internalized costs to society of the operation of the enterprise.
personal liability by attempting to rehabilitate them.\textsuperscript{183} The liquidation is premature from society's perspective because a potentially viable firm is lost and social costs arising from liquidation are incurred. From the perspective of the secured lender with a floating charge, however, value may well be maximized by an early liquidation in which it is paid a substantial recovery, even if other creditors are not.

b. Reorganization Alternatives.

While measuring success of the chapter 11 reorganization process requires a comparative analysis of liquidation alternatives, this is not the end of our inquiry. One of the principal benefits of chapter 11 is its creation of a framework against which out-

\textsuperscript{183} See Company Directors Disqualification Act 1986, ch. 46, §§ 6, 15 (Eng.). For example, English airlines, such as Laker, have been liquidated without the opportunity to reorganize, whereas United States airlines frequently rehabilitate under chapter 11. Continental, TWA, and Hawaiian are among airlines that have emerged from chapter 11. Of course some United States airlines cannot reorganize and are liquidated. Examples include Eastern and Pan American airlines. Other Western European countries that lack a reorganization law mirror the English experience. For example, the recent financial difficulties of Fokker Aircraft in the Netherlands resulted in liquidation under Dutch surséance (suspension), with the loss of 3,000 jobs. If instead Fokker were based in the United States, it could have used chapter 11 to attempt reorganization, perhaps generating 1.1 billion Guilders in additional value and saving an additional 3,000 jobs. See Johan S. Depraetere et al, "Fokker Aircraft: Creating Value through Chapter 11" (1996) (unpublished manuscript on file with author).

Unlike England and other Western European countries that developed their economy with a strong central banking system, the United States has had a weak central banking system and resorted to private markets for capital formation. See Roe, supra note 32, at 644-45. Whereas the English system favors enforcement of contractual remedies by the secured creditor, the American system has long recognized the need for all parties to sacrifice to facilitate reorganization. See Canada S. Ry. v. Gebhard, 109 U.S. 527, 536, 3 S. Ct. 363, 369 (1883) ("Every member of a political community must necessarily partake of some of the rights which . . . he might have retained. Such concessions make up the consideration he gives for the obligation of the body politic to protect him . . . . Bankrupt[cy] laws . . . are of that character."). The Supreme Court recognizes that the need for secured creditors to sacrifice remains unchanged. See United Savings Ass'n v. Timbers of Inwood Forest Assocs., Ltd., 484 U.S. 365, 379, 108 S. Ct. 626, 634 (1988) ("That secured creditors do not bear one kind of reorganization cost hardly means that they bear none of them.").
of-court negotiations proceed.\textsuperscript{184} Chapter 11 encourages expeditious, efficient out-of-court restructurings based on the participants' expectations of what would occur in a chapter 11 case if they failed to reach agreement.\textsuperscript{185} Our definition of success for the chapter 11 system must take account of its impact on out-of-court restructurings and the alteration of that system that will result from any change to chapter 11. We must recognize the dependence of these systems and account for feedback effects when one is changed.

Our analysis is complicated further by the availability of prepackaged or prenegotiated chapter 11 cases.\textsuperscript{186} Where the debtor's business operations do not need restructuring and its insolvency problem is caused by too much debt, a prepackaged or prenegotiated chapter 11 case may be the most efficient existing path to recapitalize the business.\textsuperscript{187} Any change in either the out-of-court workout system or

\textsuperscript{184} Indeed, Congress viewed chapter 11 as a remedy to be pursued after failed out-of-court negotiations. "When an out-of-court arrangement is inadequate to rehabilitate a business, the bankruptcy laws provide an alternative." House Report, supra note 7, at 20.

\textsuperscript{185} See \textit{In re} Filex, Inc., 116 B.R. 37, 41 (Bankr. S.D.N.Y. 1990) ("The Bankruptcy Code encourages workouts outside of Chapter 11. Such workouts are expeditious, because at times the formal Chapter 11 machinery may be time-consuming and expensive . . . "). Chapter 11 may be more efficient than out-of-court workouts in avoiding, \textit{inter alia}, tax costs and free-rider problems. See supra note 172.

\textsuperscript{186} See supra note 171. In a prenegotiated case, plan negotiations take place outside chapter 11, but the debtor does not formally solicit acceptances of the plan until after if files for chapter 11 relief. In the prepackaged case, both negotiation and voting occur before the debtor files for chapter 11 relief. See 11 U.S.C. § 1126(b) (1994); Fed. R. Bankr. P. 3018(b). Both the prenegotiated case and the prepackaged case are relatively speedy and inexpensive, because much of the negotiation takes place out of court and the time spent in chapter 11 is minimized. See Tashjian et al., supra note 171, at 143 ("[T]he total time to complete a prepack is . . . dramatically less than . . . the time required to complete a traditional Chapter 11 reorganization.").

\textsuperscript{187} Tashjian's data are inconclusive whether prepackaged bankruptcies are superior to traditional chapter 11 cases and out-of-court restructurings. See Tashjian et
the regular chapter 11 system will necessarily affect the utility of prepackaged chapter 11 cases. Therefore we should study the costs and benefits of the prepackaged chapter 11 process, as a subspecies of chapter 11 cases, before changing chapter 11 or the out-of-court restructuring system.


Those academics, commentators, and judges obsessed with obtaining empirical data to justify the palpable benefits of a complex, nonlinear, chaotic chapter 11 system will undoubtedly seek to quantify that part of the puzzle that easily lends itself to identifiable numerical analysis. They will want to know how long each chapter 11 case took, what percentage of the estate was distributed to secured creditors, what percentage of the estate was distributed to unsecured creditors, and what percentage of the estate was distributed to owners. In addition, they will want to know what percentage of the estate was distributed to the professionals who rendered services in the case. The statistical analysis may also inquire whether a plan of

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188 Many of these studies are referenced in Tashijian et al., supra note 171, at 136 & n.3. See generally Teresa A. Sullivan et al., The Use of Empirical Data in Formulating Bankruptcy Policy, 50 LAW & CONTEMP. PROBS. 195 (1987).

189 LoPucki and Whitford measure the market value of the distributions, arguing that "those values are better measures of the 'success' of the proceeding [sic] than data on the debtor's performance or nonperformance of the promises themselves." LoPucki & Whitford, Patterns, supra note 12, at 599 n.7.

190 E.g. Tashijian et al., supra note 171, at 136 (identifying "the length of time required to reorganize, the direct fees associated with the reorganization, the degree to which absolute priority is violated, and recovery rates by creditors" as indirect measures of efficiency).

191 See id. at 136, 143-44 (measuring direct restructuring fees as a percentage of book value of assets); Robert M. Lawless et al., A Glimpse at Professional Fees and Other Direct Costs in Small Firm Bankruptcy, 1994 U. ILL. L. REV. 847, 870; Steve H. Nickles & Edward S. Adams, Tracing Proceeds to Attorneys' Pockets (and the Dilemma of Paying for Bankruptcy), 78 MINN. L. REV. 1079, 1080-81 &
reorganization was filed and confirmed; if so, how long the chapter 11 case took from filing through confirmation; and perhaps how long it took until substantial consummation of the plan. Analysts will gather statistics to determine what percentage of chapter 11 cases resulted in confirmed plans or consummated plans. And then they will study chapter 11 cases to determine whether debtors or businesses "stay out" of chapter 11 or become recidivists.

From a methodological standpoint, the statistical approach raises three important questions: over what period of time should we measure maximization of value; what data do we collect to measure maximization of value; and if we seek completeness, how do we identify transaction costs and measure them? There are no correct easy

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A plan is substantially consummated when all property of the estate has been transferred out of the estate and distribution under the plan has commenced. See 11 U.S.C. § 1101(2) (1994).

E.g. LoPucki & Whitford, Patterns, supra note 12, at 600-01; Jensen-Conklin, supra note 192. For a commentator who argues in favor of measuring success based on consummation, see Bufford, supra note 17, at 833.

See LoPucki & Whitford, Patterns, supra note 12, at 601-04 (discussing both entity and business survival). It is possible for the business and the debtor entity to survive independently. For example, the trustee or debtor in possession could sell the business as a going concern to a new entity with all consideration distributed to creditors. The business has survived even though the debtor-entity might not. On the other hand, the trustee or debtor in possession could liquidate the business piecemeal, but the debtor-entity could use the consideration to start a new enterprise. Thus, the entity could survive even though the business did not.
answers to these questions. As a result, different researchers have approached the subject using different time frames, different data categories, and different approaches with respect to transaction costs.\textsuperscript{196}

Although many scholars have differentiated large and small chapter 11 cases,\textsuperscript{197} some critics rely on general statistics for all chapter 11 cases.\textsuperscript{198} These studies produce conclusions of limited value, because the pool of chapter 11 business reorganization cases is not homogenous. Large manufacturing companies with hundreds of jobs are combined with numerous single-asset real estate cases in statistics compiled by the Administrative Office of the United States Courts.\textsuperscript{199} The only thing these classes of cases have in common is that the debtors sought relief under chapter 11 of the Bankruptcy Code. The large case is less likely than the small case to have an identity of interest between managers and owners of the debtor. The large case is more likely than the small case to generate creditor interest because of the

\textsuperscript{196} See, e.g.,Bufford, supra note 17, at 831-33 (using corporate bankruptcy data from his 1993 cases and from Judge Lisa Hill Fenning's 1992 data base); Tashjian et al., supra note 171, at 139-40 (selecting 49 prepackaged bankruptcy cases filed from 1986 through 1993, in which they obtained copies of the plan of reorganization); LoPucki & Whitford, Patterns, supra note 12, at 598 n.4 & app. 1 (examining 43 "publicly held companies that reported at least $100 million in assets at filing in which a plan of reorganization was confirmed before March 15, 1988.").

\textsuperscript{197} E.g. LoPucki & Whitford Patterns, supra note 12, at 598 (studying 43 large, publicly held companies); Warren, Bankruptcy Policymaking, supra note 14, at 441 (noting that public companies "represent less than one-tenth of 1% of all the Chapter 11 cases" filed during the 1960s through the 1980s); White, supra note 75, at E7-34 (studying payout rate to unsecured creditors in 90 small cases). Cf. Bufford, supra note 17, at 832 (noting that we should be careful about extending recommendations for corporate chapter 11 cases to cases filed by noncorporate debtors).

\textsuperscript{198} See, e.g., supra note 160.

amounts at stake. And the large case is better able to bear the administrative expense costs of the chapter 11 process than the small case. Yet some analysts make the mistake of applying the same standards of success to all kinds of chapter 11 cases. 200

To some extent, the statistics can help us understand how chapter 11 is working. The statistics can validate, in numerical terms, whether chapter 11 is consensual, inexpensive, and free from unnecessary delay, all of which are hallmarks of success. 201 While these parameters are necessary to success, standing alone they are insufficient to substantiate conclusions regarding the success of chapter 11 in the broader social sense. There is a substantial risk that these data can be used to support analysis that purports to be consistent, objective, and amoral. But such an analysis necessarily would be incomplete and might be misleading.

5. More Appropriate Measures.

In the end, statistical analysis of quantifiable data ignores whether people subjected to the process believe that justice was done, a fair result was reached, and the parties who participated in the case and were subjected to it feel "good." This kind of unquantifiable data, as well as others mentioned above, may be as significant or even more significant than the numerical data collected by those obsessed with quantifiable statistics.

200 See supra note 198. See Bradley & Rosensweig, supra note 160, at 1078 n.80 (disclaiming application to nonpublic corporations of their empirical data for public companies, but stating that their "theoretical analysis of corporate reorganization . . . arguably applies with equal force to private companies.").

201 See, e.g., Fed. R. BANKR. P. 1001 ("These Rules shall be construed to secure the just, speedy, and inexpensive determination of every case and proceeding."); Broude, supra note 87, at 441, 454 ("chapter 11 is biased toward settlement by the parties . . . ."). See also supra part III.C.3.
In this author's view, it is appropriate to determine the objectives of chapter 11 and to evaluate the chapter system both subjectively and objectively by interpreting statistics in light of those objectives. If we limit our analysis to the quantifiable, we run a substantial risk of misguided analysis. For example, consider the statistical analysis of the criminal justice system. A commentator seeking to evaluate the criminal justice system might look at the conviction rate of defendants at trial. If the goal of the system is to convict every person who perpetrates a crime, a high conviction rate might signify success. By the same token, if the system seeks to avoid convicting even one innocent person, a high conviction rate is indeterminate at best and indicative of failure at worst. And if the goal of the system is to decrease the crime rate or deter potential criminals, a high conviction rate tells us nothing about success.

In the same way, if the goal of chapter 11 is to encourage expeditious and consensual out-of-court workouts, a high plan confirmation rate does not necessarily indicate success; debtors who desire to restructure successfully might avoid bankruptcy entirely. On the other hand, if we consider the goal of chapter 11 to be to resuscitate as many critically ill businesses as possible, a confirmation rate of ten or twenty percent might signal success. 202

202 According to the Statistical Analysis and Reports Division of the Administrative Office of the United States Courts, "the overall confirmation rate for chapter 11 cases filed prior to 1987 was about 17%, and that rate had been rising steadily." See Ed Flynn, Statistical Analysis of Chapter 11, at 10 (Oct. 1989) (citing study performed for the Administrative Office by Ernst & Young, Inc.) (unpublished memorandum from Bankruptcy Judges Division of Administrative Office of the United States Courts, on file with author). "It appears that approximately 22.4% of the cases filed in 1986 have been or will be confirmed." Id.

Perhaps the better way to proceed is to agree on fundamental objectives for chapter 11 business bankruptcy cases and then to use pattern recognition techniques to exclude from the statistical analysis those cases that do not appear to meet those objectives.\textsuperscript{203} Then we can use the remaining data to focus more precisely on success.

For example, suppose chapter 11 has as one of its principal objectives the preservation of jobs. It may be that in the single-asset real estate case, very few jobs are lost whether the case is confirmed or the lender is permitted to foreclose.\textsuperscript{204} On the other hand, in the large manufacturing case, preservation of the enterprise as a going concern maintains jobs, while liquidation of the business may well result in a loss of jobs in the community, the state, or the United States.\textsuperscript{205} Even if liquidation results in no net reduction in jobs, transaction costs may be involved in shifting the work force from one set of workers to a new set. Thus the benefit of chapter 11 in the manufacturing context may far exceed the benefit in the single-asset real estate case.

\textsuperscript{203} One of the benefits of chaos theory is that it permits pattern recognition of phenomena that are impossible to describe mathematically because of their complexity and turbulence. Judge Fenning has suggested a pattern recognition approach to chapter 11 cases, but has not acknowledged the fuzziness of the edges where prediction is problematic or impossible. See Fenning, supra note 14, at 114-15.

\textsuperscript{204} In "single asset real estate cases . . . the only consequence of liquidation is the owners' loss of their investment and expectancy of a return. Typically, there are no employees, customers, inventory or, for that matter, even unsecured creditors." Ponoroff, supra note 14, at 462 n.67. Judge Fenning has predicted, in "[g]azing into the crystal ball for the 21st Century," that "[w]ith rare exception, single asset real estate cases will be history." Fenning, supra note 14, at 114, 117.

\textsuperscript{205} Even if the business continues to operate, business reorganization can lead to loss of jobs if a business combination occurs or jobs are shifted overseas. This presumes, of course, that we choose to define maximization of value on a national rather than an international basis.
context. If this is so, it is certainly inappropriate to apply the same standard of success to these different kinds of cases.

The same conclusion would follow if the objective of chapter 11 were to preserve synergistic enterprises. The large manufacturing case is likely to have synergy, whereas the single-asset case may not. It is probably inappropriate to consider these kinds of debtors in the same statistical pool. A comparative analysis, however, might lead to the conclusion that chapter 11 should be available only for service, manufacturing, or distribution businesses, where significant numbers of jobs are at stake and synergy exists, and should not apply to single-asset real estate cases, where these factors are absent. Alternatively, one might conclude that single-asset real estate cases should remain eligible for chapter 11 relief, not to promote synergy, but to prevent forfeiture of the asset to a secured lender under a nonbankruptcy law system that is suboptimal.

We could take a similar approach to large cases and small cases based on the likelihood of creditor participation and the absence of creditor interest. If one of the premises of chapter 11 is negotiation of a consensual plan based on input from and negotiation with creditors, and we find that creditors do not participate in smaller

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206 Indeed, numerous courts routinely dismiss or display hostility toward single-asset real estate cases. See Janet Flaccus, Have Eight Circuits Shorted: Good Faith and Chapter 11 Bankruptcy Petitions, 67 AM. BANKR. L.J. 401, 405-06 n.24 (1993) (collecting opinions in which courts dismissed cases or granted relief from the automatic stay to the secured creditor and comparing them with those where the court did not dismiss the case or grant relief from stay).

207 Judge Bufford reminds us that concentration of real estate in the hands of foreclosing financial institutions was a factor that influenced the length and depth of the Great Depression. Bufford, supra note 17, at 843-44.
cases, perhaps we should exclude smaller cases from chapter 11 rather than using statistics gathered in smaller cases to argue that chapter 11 is a failure and should be scrapped altogether. Alternatively, we could apply a different standard of success to evaluate the smaller chapter 11 cases and to propose a separate system for these cases, if appropriate.

7. Analyzing The Residue.

Once we have defined an appropriate data pool, it becomes important to identify parameters that will measure or approximate success against the goal of maximization of social enterprise value (or net social value) through chapter 11, in comparison with alternative possibilities. This part begins by discussing some popular measures of success that may provide us with inconclusive data.

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208 Although chapter 11 is premised on creditor participation and negotiation with the debtor, often creditors are unwilling to participate in small business cases. See generally Lynn M. LoPucki, The Debtor in Full Control—Systems Failure Under Chapter 11 of the Bankruptcy Code (pt. 2), 57 AM. BANKR. L.J. 247,247 (1983).


210 Commentators consider chapter 11 to be more successful for public companies than for nonpublic companies. See, e.g., Lynn M. LoPucki, Chapter 11: An Agenda for Basic Reform, 69 AM. BANKR. L.J. 573, 574-76 (1995); Warren, Bankruptcy Policymaking, supra note 14, at 373-74 & nn. 98-100. Ideally the data would be tabulated separately for large cases and small cases.

211 Commentators have alleged that chapter 11 is too expensive for the small corporation. See, e.g., Alexander L. Paskay & Frances P. Wolstenholme, Chapter 11: A Growing Cash Cow, Some Thoughts on How to Rein in the System, 1 AM. BANKR. INST. L. REV. 331, 346 (1993). If so, perhaps a different standard of success is appropriate if society determines to allocate resources to save these small businesses. See infra notes 229-30 and accompanying text. Professor Korobkin has advocated the establishment of a Small Business Bankruptcy Board to determine the viability of small cases at the outset of a chapter 11 filing. Korobkin, Vulnerability, supra note 209, at 431.
a. **Confirmation Data Are Inconclusive.**

Traditional analysts will ask whether a plan was filed, whether it was confirmed, and whether confirmation was consensual.\(^{212}\) Certain parameters, such as whether a chapter 11 plan was "confirmed," will have superficial appeal but doubtful statistical validity. For example, data based on confirmation of a chapter 11 plan are likely to be both over- and underinclusive. The standard is overinclusive because a confirmed plan may include a liquidation plan or a plan that is optimistically feasible, but likely to cause the business to reenter the chapter 11 process, restructure, or liquidate within a short period after confirmation. The standard is underinclusive because often a successful settlement can result in dismissal of the chapter 11 case or the sale of all assets of the business outside the context of a plan. This argument does not mean that confirmation of the plan is unimportant in measuring success, just that statistics based on confirmation may be misleading. We should be more interested in determining whether chapter 11 helped rehabilitate a business that remained viable for a significant period following confirmation than determining whether the case resulted in a confirmed plan.

b. **Cost Variables Are Inconclusive.**

Another parameter analyzed by commentators is the percentage of the estate distributed to professionals in fees and costs.\(^{213}\) Certainly the transaction costs of administering the chapter 11 system are significant. Once a chapter 11 case begins for an enterprise, the complexity of the case often is directly correlative with the absolute

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\(^{212}\) See, e.g., *supra* notes 188-195 and accompanying text.

\(^{213}\) See *supra* note 191 and accompanying text.
amount of professional fees incurred.214 In addition, the magnitude of professional fees will be determined by whether the case follows a litigious or negotiated path. Of course, the chapter 11 process is not bimodal. Cases that start down a litigation path can lead to negotiated settlements.215 And the factors that tip a case from consensual resolution into litigation can be numerous, unquantifiable, and chaotic.216 Thus many factors bear on the magnitude of professional fees in a chapter 11 reorganization case.

Even though some of the factors are unquantifiable and not susceptible to analysis, we can calculate the overall amount of the fees at the conclusion of the case. But we cannot use these data to determine whether chapter 11 is successful unless we perform an efficiency analysis: Were the services necessary? Could the results have been achieved more expeditiously? Could better results have been achieved? Answering these questions requires a detailed inquiry based on the facts of a particular case. An analyst would have considerable difficulty developing a simple model to fairly determine and compare efficiency in different chapter 11 cases, even if the cases were remarkably similar, because the chapter 11 process is not equivalent to a repetitive

214 To some extent, based on the complexity involved, the magnitude of the professional fees will bear little relation to the amount of debt, assets, sales, or other financial measures involved in the case. It is true, however, in the author's experience, that in cases with limited assets, professional fees tend to diminish because of the lack of assets available to pay fees and the propensity of courts to cut them if they become too large a percentage of the assets of the estate.

215 Unlike the traditional bilateral lawsuit, the chapter 11 process can consist of numerous conflicts and disputes, any one of which can erupt into full-blown litigation.

216 For example, a personality dispute may trigger litigation, and the source of the dispute need not originate among the professionals. It may occur only among the business people or among the business people and professionals. The proclivities of the judge may foster or diminish prospects of litigation. The general economic conditions and amount of work available for the professionals can foment or dampen litigation.
scientific experiment. Rather, slight variations in unquantifiable variables can lead to remarkably different results. Stated differently, chapter 11 is nonlinear, and efforts to measure it on a linear basis are doomed to fail.

We also must remember that the debtor would incur some professional fees in pursuit of any alternative to chapter 11. We know that lower fees are better than higher fees (except for the recipient), but we do not know whether it is possible or reasonably likely to obtain a comparable result with lower fees. Therefore considering the absolute level of professional fees paid in a particular case is likely to be inconclusive whether the case was successful.

c. Distribution Percentages Are Inconclusive.

Similar defects exist with respect to many of the other variables that have been used traditionally to analyze success in chapter 11. For example, looking at the percentage recovery by creditors can be quite misleading. Certainly it is important to creditors to know what percentage on the dollar they are receiving in a chapter 11 case. But from the standpoint of analyzing success, the inquiry from a societal viewpoint should be what creditors would have received had there been no chapter 11 case, taking into account transaction costs and the time value of money. Thus the relevant inquiry should be whether, on a net present value basis, creditors are better off under the chapter 11 plan than they would have been in the absence of chapter 11.

\[ \text{See supra note 14.} \]

\[ \text{See, e.g., LoPucki & Whitford, Bargaining Over Equity’s Share in the Bankruptcy Reorganization of Large, Publicly Held Companies, 139 U. Pa. L. Rev. 125, 141-43, 164-68 (1990).} \]
Even that inquiry might not be wholly satisfactory. Consider the rare chapter 11 plan that pays creditors in full with postpetition interest.\textsuperscript{219} Even though creditors are economically no worse off than they would be in the absence of bankruptcy (and may be better off),\textsuperscript{220} the delay imposed on creditors by the chapter 11 process may render the case unsuccessful from their standpoint,\textsuperscript{221} and the cost to process the case through the system might render it unsuccessful from a societal perspective.

\textbf{d. Factors That Measure Business Viability Are Useful.}

Even though we recognize the chapter 11 process is nonlinear and difficult to evaluate, there are variables we should examine to help our measurement of success.


\textsuperscript{220} Certain unsecured creditors who are paid in full with interest may be better off in chapter 11 because some might not have received full payment outside of chapter 11 if other creditors had pursued state remedies. For example, a secured creditor with a lien on all of the debtor's assets could foreclose and sell the assets at a distressed price far below the going concern value of the assets in a chapter 11 case. Even if the debtor has no secured creditors, the same result may follow: certain unsecured creditors could obtain judgments expeditiously and levy on assets to receive full payment, while other creditors who obtain judgments later would find no assets remaining and receive nothing.

\textsuperscript{221} Creditors might be harmed by delay for several reasons. For example, the debtor's failure to make timely payments might cause creditors to write down loans and have to dedicate reserves for possible losses. Even if the creditor is paid in full later, it has lost the opportunity to make alternative investments. The delay in payment might also deprive the creditor of the chance to make a profitable investment where its opportunity cost exceeds the rate of return it will receive on its claim against the debtor. See United Sav. Ass'n v. Timbers of Inwood Forest Assocs., Ltd., 484 U.S. 365, 108 S. Ct. 626 (1988) (holding that unsecured creditor is not entitled to adequate protection for delay and lost opportunity cost caused by chapter 11).
Variables that measure the viability of the rehabilitated business might be indicative of success or failure of the chapter 11 process. A successful chapter 11 case would produce a business that is well capitalized to compete in the market. The rehabilitated business would not be overleveraged; that is, it would have a suitable debt/equity ratio for its industry, and its current assets would exceed its current liabilities by a comfortable margin.222 The rehabilitated business would have the durability to withstand an economic downturn; adequate capital sources and cash flows are indicative of this aspect of success.

Another indicator of success is the resumption of trade credit. If trade creditors are extending unsecured trade credit on ordinary trade terms to the rehabilitated company, chances are good that the chapter 11 case has been successful.

Finally, we should determine whether the rehabilitated business has ordinary bank lines and access to the public or private debt and equity capital markets. Market confidence is a good indicator that the business is poised to expand, which is a good measure of successful rehabilitation.

e. **Ex Post Evaluation Of Justice, Speed, And Expense Is Warranted.**

Based on our definition of success, evaluation of economic-based market data alone is insufficient. We should instead undertake an ex post analysis of the relative justice, speed, and expense of the chapter 11 case. We should also analyze the flexibility and adaptability of chapter 11 ex post. We could gather this information from

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random samples of chapter 11 cases by examining case files and conducting interviews with key business people and professionals in each case. Although this information necessarily will be subjective, it can help us discern patterns in chapter 11 cases to help us refine our notions of success. We might learn that speedy, inexpensive cases lead to unjust results or that longer, more expensive cases lead to negligible justice gains.

f. We Should Study The Workout System.

Finally, we should attempt to measure the success of the chapter 11 system by looking at its shadow. We know that out-of-court restructurings are conducted in the shadow of chapter 11.\textsuperscript{223} We should interview business people and professionals who have participated in out-of-court restructurings to determine the impact of chapter 11 on that process. The results should enhance our understanding of the unique role of chapter 11 and help us evaluate its success.

To this point, this article has proposed a rough definition of success that is likely to change over time, based on feedback and the evolution of the chapter 11 system. This article concludes by suggesting what we can do with data on success once we have analyzed it.

V. Using Success to Move Toward Reform.

This part uses the definition of success to discuss proposals to reform the chapter 7 and chapter 11 business bankruptcy systems.\textsuperscript{224} This part suggests reforms to improve the efficiency of the system to maximize economic value and social value.

\textsuperscript{223} See supra notes 184-85 and accompanying text.

One way Congress might improve the business bankruptcy system is to amend the Bankruptcy Code to deter fraud in chapter 7 and chapter 11 cases. Perhaps Congress could improve the system by requiring private trustees or the Office of United States Trustee to investigate exhaustively a certain number of debtors per year. Even if trustees conducted only 100 investigations per year, the in terrorem factor could lead to a more accurate disclosure of assets by debtors in other cases. And if the investigations should reveal fraudulently transferred or secreted assets, a timely prosecution or two could have a useful deterrent effect to make the system more successful going forward.225

Congress should also amend the Bankruptcy Code to deal better with the cost of administering chapter 11 cases. Perhaps the chapter 11 system could be more successful if it had a threshold requirement admitting only those businesses that are good candidates to bear the cost of the chapter 11 process and emerge rehabilitated. We could achieve this goal either by excluding types of businesses that are unlikely to qualify, or by requiring the court to determine whether to approve the filing early in the chapter 11 process.226 Alternatively, we could require all companies to pay a higher flat access fee to utilize the system. Where a consensus develops that the transaction costs of the chapter 11 process for a category of cases will exceed the benefits of

225 Not surprisingly, secreting assets from the bankruptcy trustee is a criminal offense. 18 U.S.C. §§ 152, 157 (1994).

chapter 11 beyond a reasonable doubt, we should either find a way to reduce the transaction costs or exclude those cases from the chapter 11 process.\textsuperscript{227}

As previously suggested, we might exclude cases where the dollar amount of assets or liabilities is too small to make chapter 11 worthwhile.\textsuperscript{228} Since the amounts at stake are small, creditors are unlikely to police chapter 11 debtors and to become involved in plan negotiations. If we are willing to devote the resources to cause the government to monitor the process, perhaps the Office of United States Trustee could act as a compliance officer. The United States trustee would monitor the debtor in possession to determine that the debtor is operating a business properly and filing business reports promptly; if not, the United States trustee could move promptly to convert the case to chapter 7, where the business would be liquidated. Another option is to return the judge to the administrative process. The judge would hold a viability hearing early after the small case is filed. If the business shows prospects for survival, the judge could set a time within which the plan would be filed.\textsuperscript{229} If not, the judge could convert the case to chapter 7 or dismiss the case, whichever is in the best interest of creditors and the estate.\textsuperscript{230}


\textsuperscript{228} For a view that small businesses add intangible value to the community and deserve special protection, see Karen Gross, \textit{Taking Community Interests into Account in Bankruptcy: An Essay}, 72 WASH. U. L.Q. 1031, 1032-35 (1994).

\textsuperscript{229} Under the Bankruptcy Code, the judge can act \textit{sua sponte} to order the debtor to file a plan by a date certain. See 11 U.S.C. §§ 105(d)(2)(B)(i), 1112(b)(4) (1994).

We also might exclude categories of cases, such as single-asset real estate cases, where the objectives of chapter 11 are unlikely to square with the facts of the case. Of course, one person's single-asset real estate case is another person's going business. While Congress might agree on clear-cut cases to exclude undeveloped raw land and to include large hotels and casinos, it would be difficult to establish a bright line somewhere in between. Is the strip center, shopping mall, partially developed project, or bed-and-breakfast inn a good candidate for chapter 11 or not? The chapter 11 data will not be wholly dispositive of this question. Is adoption of a "no equity" test as a basis for relief from the automatic stay a better remedy than excluding categories of single-asset real estate debtors from chapter 11?

VI. Conclusion.

By defining success in business bankruptcy cases, we can help make the process less expensive, more consensual, and more efficient. We can also optimize value for society.

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232 Under the Bankruptcy Code, a secured creditor is entitled to relief from the automatic stay if the creditor proves a lack of adequate protection of its interest in the collateral or if it shows both that the estate lacks equity in the collateral and that the collateral is not necessary to an effective reorganization. 11 U.S.C. § 362(d)(1)-(2) (1994). Congress added a third basis for relief from stay in single-asset real estate cases filed on or after October 22, 1994. Id. § 362(d)(3) (as added by the Bankruptcy Reform Act of 1994, Pub. L. No. 103-394, § 218(b), 108 Stat. 4106, 4128). Perhaps we should consider granting the secured party relief from the automatic stay in single-asset real estate cases if the creditor proves that the estate lacks equity in the property whether or not it is necessary to an effective reorganization.
More than 20 years ago Professor Countryman challenged himself to define an executory contract.\textsuperscript{233} He compared the process to sculpting an elephant from a block of stone: You simply chip away anything that doesn't look like an elephant.\textsuperscript{234} Perhaps that is the best approach to measuring success in chapter 11 business reorganization cases. Let us begin by chipping away at anything that does not look like a successful chapter 11 business reorganization case. The results in the remaining cases may be sufficiently positive and coherent that we can reach a consensus with respect to the unquantifiable, intangible variables and benefits that account for the success of chapter 11.


Appendix

This article conceptualizes social enterprise value without providing a precise formula to calculate the quantifiable portion of the concept or providing a philosophical basis to balance its quantifiable and unquantifiable components. This Appendix briefly addresses these issues and concludes that the comparison of costs and benefits of pursuing alternatives to reorganization is the critical comparison. Reorganization should proceed unless the benefits of pursuing an alternative outweigh its costs, including the loss of any net benefits of reorganization.

I. Quantifiable Social Enterprise Value.

Derivation of a useful quantifiable social enterprise value requires scrupulous attention to the costs and benefits that would result if the debtor were not rehabilitated. For illustrative purposes, suppose the alternative to reorganization is liquidation. Consider the following definitions:

SEV = Social Enterprise Value of the debtor as a going concern
SLV = Social Liquidation Value of the liquidated debtor
EV = Quantifiable Enterprise Value of the debtor
MV = Economic or Market Value of the debtor

\[ \text{The model can be expanded to deal with other alternatives to reorganization under chapter 11. For example, if the alternative were out-of-court restructuring, the comparison would be to out-of-court costs and benefits instead of to liquidation costs and benefits. In practice, the model would deal with each reasonable alternative to reorganization, i.e., merger, sale, split up, spin off, liquidation, etc.} \]

\[ \text{The model assumes that the most efficient form of liquidation is the alternative used to compare with reorganization under chapter 11.} \]
EX = Quantifiable Externalities and Spill-over Effects

LC = Liquidation Costs

LB = Liquidation Benefits

Enterprise Value consists of the economic or perfect market value of the debtor, as adjusted to account for quantifiable Externalities or Spill-over effects that are imposed by the debtor as a going concern. Thus EV = MV - EX.

But EV does not accurately reflect the value of the debtor to society, because the debtor’s existence and operation might avoid second-order effects that would occur if the debtor were liquidated. For example, liquidation of the debtor might trigger distressed asset values, liquidation costs, severance benefits, retraining costs, unemployment benefits, and other transaction costs or externalities of liquidation.237 Therefore the debtor’s Social Enterprise Value should be augmented by these liquidation costs, LC, which are avoided by the debtor’s rehabilitation. As demonstrated below, it is unnecessary that LC excludes any avoided costs that are incorporated directly into EV.

The debtor’s liquidation can also result in benefits, LB, that are not realized when the debtor continues in operation. For example, where the debtor’s assets can be redeployed to a higher and better use, liquidation might result in a net benefit to society.238 Therefore the debtor’s Social Enterprise Value should be diminished by

237 Of course some of these externalities could be positive in which case Social Enterprise Value would be reduced by these liquidation benefits. For example, severance benefits and retraining costs might produce a net social benefit by developing a workforce with greater skills at nominal cost.

238 Even if the property were to lie fallow for a while, society might realize some benefit from the debtor’s liquidation, where the debtor’s continued operation would have created environmental or other tort liabilities.
these liquidation benefits, LB, which are not realized by the debtor's rehabilitation. As demonstrated below, it is not necessary that LB excludes any avoided benefits that are incorporated directly into EV. Therefore, to determine Social Enterprise Value for a debtor, calculate the Enterprise Value, augment it by avoided Liquidation Costs, and diminish it by unrealized Liquidation Benefits: SEV = EV + LC - LB.

To evaluate the most efficient liquidation alternative, we compute Social Liquidation Value. Logically, Social Liquidation Value should equal the value of the debtor as a going concern, EV, augmented by liquidation benefits, LB, and diminished by liquidation costs, LC. Thus SLV = EV + LB - LC.

An optimal system would liquidate the debtor when SLV > SEV.239 Simplifying, the inquiry is whether (EV + LB - LC) > (EV + LC - LB). Subtracting EV from both sides yields (LB - LC) > (LC - LB). Transposing and dividing by 2 the question becomes whether LB > LC. If the Liquidation Benefits are greater than Liquidation Costs, then liquidation of the debtor is preferable to reorganization, and vice versa.

Since EV drops out of the inquiry, the relative level of EV is irrelevant. Likewise it is important that LC and LB include all costs and benefits of liquidation, even if they are included in EV. To avoid double counting, it is only necessary that LC not include a cost that is also included in LB as a negative benefit, and vice versa. Maximization of quantifiable Social Enterprise Value occurs through reorganizing the debtor whenever LB < LC.

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239 If SEV is greater than SLV, then reorganization is optimal.
II. Unquantifiable Social Enterprise Value.

Of course not all aspects of Social Enterprise Value are quantifiable. Liquidation Costs or Liquidation Benefits may be unquantifiable because they are indeterminate or determinable only at great cost. Theoretically, it is important to compare quantifiable and unquantifiable Liquidation Costs with quantifiable and unquantifiable Liquidation Benefits. But since the unquantifiable costs and benefits are not quantified, the comparison cannot be mathematical.\textsuperscript{240}

This author prefers to weigh the unquantifiable Liquidation Costs and Liquidation Benefits by referring to social morals, mores, and values.\textsuperscript{241} The comparison of unquantifiable Liquidation Costs and Liquidation Benefits will necessarily be subjective, which raises difficulties in balancing these aspects of Social Enterprise Value with quantifiable aspects. Although it is possible to regard the quantifiable outcome as predominant and to use the unquantifiable outcome as determinative only when the economic inquiry is close or inconclusive, such an approach diminishes the importance

\textsuperscript{240} Mathematics does try to mix real and imaginary numbers, but not with determinative results in all instances. For example, where the imaginary number $i = \sqrt{-1}$, we know that $(2 + 2i) > (1 + i)$. But we cannot determine whether $(2 + i) > (1 + 2i)$. Some unquantifiable aspects of SEV are intangible; assigning a value to them becomes at best subjective and at worst meaningless. Economists try to quantify everything by estimating unquantifiable variables; this technique enables them to appear to make decisions based on an amoral, mathematical, efficiency analysis. Their value judgments are made, however, in the estimation process and in their aggregation of individual preferences on a weighted or equal basis. This author prefers to acknowledge the human process whereby judges and entrepreneurs make judgments based on fuzzy values and intuition. We should analyze this process of balancing apples and oranges instead of trying to convert apples to oranges.

\textsuperscript{241} See supra note 166 and text accompanying notes 166-167.

of the unquantifiable components of Social Enterprise Value.\textsuperscript{242} Unquantifiable aspects of Social Enterprise Value should be accorded equal weight to quantifiable aspects, just as Yin and Yang balance each other in Chinese philosophy.\textsuperscript{243} Just as judges determine whether conduct satisfies due process of law or constitutes cruel and unusual punishment,\textsuperscript{244} so too will judges determine whether the unquantifiable and quantifiable aspects of Social Enterprise Value support reorganization or liquidation of the debtor. Courts evaluating the 8th amendment to the Constitution do not measure the mathematical frequency of punishment and regard cruelty as an afterthought. Nor should courts ignore whether the chapter 11 system leads to a reorganization result that is just, flexible, adaptable, and the like.

\textsuperscript{242} See supra notes 35-37 and accompanying text.


\textsuperscript{244} See U.S. CONST., amends. V, VIII, & XIV.