

BOSTON COLLEGE

INDUSTRIAL AND COMMERCIAL LAW REVIEW

VOLUME XVIII

MARCH 1977

NUMBER 3

THE ROLE OF THE SECURITIES AND EXCHANGE COMMISSION UNDER CHAPTER X, CHAPTER XI AND PROPOSED AMENDMENTS TO THE BANKRUPTCY ACT

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Chapters X¹ and XI² of the Bankruptcy Act³ seek to effectuate the rehabilitation of corporate debtors⁴ by means of a unique collaboration between the federal district court and the Securities and Exchange Commission (SEC or Commission).⁵ Chapter X reorganizations involve "the judicial process whereby both unsecured and secured debt, as well as the interests of stockholders, may be adjusted, modified or otherwise dealt with."⁶ In contrast, Chapter XI arrangements comprise simpler, more expedited procedures for the settle-

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¹ Bankruptcy Act, §§ 101-276, 11 U.S.C. §§ 501-676 (1970).

² *Id.*, §§ 301-399, 11 U.S.C. §§ 701-799 (1970).

³ 11 U.S.C. §§ 1-1255 (1970).

⁴ 6 COLLIER ON BANKRUPTCY, ¶ 0.09 at 99 (14th ed. 1972) [hereinafter cited as COLLIER]; 8 COLLIER, ¶ 2.09 at 82-84. Petitions proposing an arrangement under Chapter XI may also be filed by an individual. *Id.* at 84.

⁵ See 2 L. LOSS, SECURITIES REGULATION 754-55 (2d ed. 1961) [hereinafter cited as LOSS]. An extensive report issued by the SEC was an important factor prompting the enactment of the Chandler Act. SECURITIES AND EXCHANGE COMMISSION, REPORT ON THE STUDY AND INVESTIGATION OF THE WORK, ACTIVITIES, PERSONNEL AND FUNCTIONS OF PROTECTIVE AND REORGANIZATION COMMITTEES, Parts I-VII (1939-40) [hereinafter cited as SEC PROTECTIVE COMMITTEE STUDY]. See REPORT OF THE SECURITIES AND EXCHANGE COMMISSION ON PROPOSED BANKRUPTCY LEGISLATION (S. 235 & S. 236), submitted to Subcommittee on Improvements in Judicial Machinery, Senate Committee on the Judiciary, December 8, 1975, at 3 [hereinafter cited as SEC REPORT ON PROPOSED LEGISLATION]; Comment, *The Issuance of Securities in Reorganizations and Arrangements under the Bankruptcy Act and the Proposed Bankruptcy Act*, 36 OHIO ST. L.J. 380, 385 (1975). At least one commentator has suggested that so many of the proposals advanced by the Commission were incorporated into the Chandler Amendments that Chapter X can be described as largely the work of the SEC. See Rostow & Cutler, *Competing Systems of Reorganizations: Chapters X and XI of the Bankruptcy Act*, 48 YALE L.J. 1334, 1335 (1939).

⁶ 6 COLLIER, *supra* note 4, ¶ 0.09 at 99-100 (footnote omitted).

ment, satisfaction or extension of unsecured debts.⁷ In each case, however, the statute contemplates procedures, short of bankruptcy, which conserve the going-concern values of the debtor's property and avoid foreclosures and forced sales.⁸ Far from liquidating the business, Chapters X and XI are designed to facilitate its continued operation, while at the same time affording full consideration to the claims of stockholders and creditors.⁹

Because Chapters X and XI contemplate the continued operation of the debtor corporation, reorganization proceedings are only "incidentally" law suits.¹⁰ Instead, the rehabilitation of the debtor presents "an administrative problem in the solution of which the public, as well as the litigants, have an interest."¹¹ A corporate reorganization, therefore, is "primarily an exercise in corporate finance and management,"¹² which necessitates a searching inquiry into broad economic and business issues, including

general economic factors, competitive conditions in the industry, its trend of demand, . . . its price policies, . . . the quality of the debtor's management[,] . . . earnings in the past, . . . prediction of future earnings, and . . . a determination of what would constitute a sound capitalization and financial structure.¹³

To resolve this fundamentally "administrative" problem, the Bankruptcy Act envisions repeated resort, by the court and other parties in interest, to the expertise of the Securities and Exchange Commission.¹⁴ Ultimate authority rests with the bankruptcy court

⁷ Bankruptcy Act, § 306(1), 11 U.S.C. § 706(1) (1970). See 8 COLLIER, *supra* note 4, ¶ 2.07[3] at 77.

⁸ 6 COLLIER, *supra* note 4, ¶ 0.11 at 116-17. Thus, the corporate debtor is only liquidated through ordinary bankruptcy proceedings in the event of the failure of the reorganization or arrangement. See Bankruptcy Act, §§ 327, 376, 377, 386(1), 11 U.S.C. §§ 727, 776, 777, 786(1) (1970) (Chapter XI cases); Bankruptcy Act, § 238, 11 U.S.C. § 638 (1970) (Chapter X).

⁹ 6 COLLIER, *supra* note 4, ¶ 0.11 at 116-17. The SEC seeks to protect not only those investors holding securities in corporations reorganized under the Act, but also those offered securities issued in the course of the reorganization proceedings. SEC REPORT ON PROPOSED LEGISLATION, *supra* note 5, at 4. Similarly, in its advisory role, the Commission looks beyond the particular plan proposed to assist the court in effectuating "uniform principles and practices." *Id.*

¹⁰ SEC PROTECTIVE COMMITTEE STUDY, *supra* note 5, at 898-902 (part I, 1937).

¹¹ Frank, *Epithetical Jurisprudence and the Work of the Securities and Exchange Commission in the Administration of Chapter X of the Bankruptcy Act*, 18 N.Y.U.L.Q. REV. 317, 321-22 (1941) [hereinafter cited as Frank].

¹² SEC PROTECTIVE COMMITTEE STUDY, *supra* note 5, at 1 (part VIII, 1937).

¹³ *Id.* at 1-2.

¹⁴ Resort to administrative expertise in judicial reorganizations did not commence with the enactment of Chapters X and XI. See Frank *supra* note 11, at 322-23 (discussing function of Interstate Commerce Commission in railroad reorganizations and responsibilities of SEC in reorganization of any registered public utility holding company). Both Chapters expressly provide for SEC intervention. Bankruptcy Act, §§ 208, 328, 11 U.S.C. §§ 608, 728 (1970). See text at notes 24-33 & 154, 159-70 *infra*.

SEC ROLE IN BANKRUPTCY

which, under the statute, may exercise extensive powers,¹⁵ including the authority to approve and confirm the arrangement or plan of reorganization.¹⁶ The Commission's role, on the other hand, resembles that of an *amicus curiae*.¹⁷ Its function is advisory, rather than adjudicative, and thus differs radically from that under those statutes which it administers.¹⁸ It neither initiates the proceedings, nor holds hearings on the plan and entertains no authority to decide the issues presented.¹⁹ Instead, the SEC's chief function is to act as an impartial representative of public investors and to provide expert assistance to the court.²⁰

This article seeks to assess the character of the SEC's role in both Chapters X and XI. The isolation of the issues which have caused the SEC particular concern, as well as the exploration of the positions it is likely to take, should enable the parties to anticipate problems arising in the course of a corporate reorganization which are likely to trigger SEC intervention. This sensitivity to the prospect of SEC intervention, in turn may permit the parties, through advance planning, to resolve issues in a manner which will forestall such intervention and thereby expedite the debtor's rehabilitation. Furthermore, the evaluation of the SEC's participation will provide the necessary conceptual framework for a critique of pending legislation which proposes sub-

¹⁵ 6 COLLIER, *supra* note 4, ¶ 0.09 at 100. *E.g.*, Chapter X: To issue stays and injunctions, Bankruptcy Act, §§ 113, 116(4), 148, 11 U.S.C. §§ 513, 516(4), 548 (1970); to issue extraterritorial process, *id.*, § 2a, 11 U.S.C. § 11(a) (1970); to appoint a receiver prior to the approval of the petition, *id.*, § 112, 11 U.S.C. § 512 (1970) (by virtue of *id.*, § 2a(3), 11 U.S.C. § 11a(3) (1970)); to exercise the jurisdiction of a court of equity, *id.*, § 115, 11 U.S.C. § 515 (1970); to permit the rejection of executory contracts and leases, *id.*, § 116(1), 11 U.S.C. § 516(1) (1970); to authorize the lease or sale of any part of the debtor's property, *id.*, § 116(3), 11 U.S.C. § 516(3) (1970); to provide for the mandatory preparation of schedules and lists of the debtor's creditors and stockholders, *id.*, §§ 163-166, 11 U.S.C. §§ 563-66 (1970).

¹⁶ *Id.*, §§ 221, 361 11 U.S.C. §§ 621, 761 (1970).

¹⁷ 6 COLLIER, *supra* note 4, ¶ 0.09 at 105. *See* Herzog, *Reorganizations and Arrangements under Chapters X and XI: Problems of Administration From the Standpoint of the Court*, 35 REF. J. 113, 116 (1961).

¹⁸ 38 SEC ANN. REP. 113 (1972). The federal securities laws authorize the SEC to hold hearings, to issue rules and to impose remedial administrative sanctions. *See, e.g.*, § 19 of the Securities Exchange Act of 1934, 15 U.S.C. § 78s (1970) (administrative sanctions with respect to exchanges and securities); *id.*, § 21, 15 U.S.C. § 78u (1970) (subpoena power in conducting investigations of alleged violations); *id.*, § 22, 15 U.S.C. § 78v (1970) (hearings); *id.*, § 23, 15 U.S.C. § 78w (1970) (power to make rules and regulations).

¹⁹ 38 SEC ANN. REP. 113 (1972).

²⁰ To fulfill its advisory role in Chapter X and XI cases, the SEC maintains a special Corporate Reorganization Division, staffed with attorneys and financial analysts, based in Washington and four of its regional offices. From 1938-1975, the SEC participated in 603 Chapter X proceedings, involving aggregate liabilities of approximately \$5.5 billion, SEC REPORT ON PROPOSED LEGISLATION, *supra* note 5, at 4. This work is accomplished at "comparatively modest cost." *Id.* In 1975, for example, combined salaries, travel and other expenses totalled \$827,027 for staffing computed as equalling 35.1 man years. *Id.*

stantial alterations of the Commission's current role in business reorganization proceedings.

I. CHAPTER X REORGANIZATIONS

A. Notice to the SEC and its Decision to Intervene

Chapter X reorganizations are initiated by the filing of a petition²¹ which must be approved by the court.²² Copies of the original petition, as well as all notices subsequently mailed to creditors, must be sent to the SEC.²³ This information enables the SEC to monitor all developments affecting the rights of public stockholders and creditors and to decide whether or not to intervene in the case.²⁴ In order to conserve its financial and human resources, the SEC restricts its discretionary involvement to proceedings which affect substantial public investor interest.²⁵ Accordingly, it is less likely to participate in a case involving only trade or bank creditors, and is more inclined to intervene where "an unfair plan has been or is about to be proposed, public security holders are not represented adequately, the reorganization proceedings are being conducted in violation of important provisions of the Act, [or] the facts indicate that the Commission can perform a useful service . . ."²⁶ Even where the Commission does not intervene on its own motion, the court may request it to make an appearance.²⁷

Once the Commission intervenes in a case, it becomes a "party in interest, with the right to be heard on all matters arising in such proceeding . . ."²⁸ As a party in interest, the Commission is represented at all hearings and it files legal memoranda to support its position on

²¹ A voluntary petition may be filed by the debtor. Bankruptcy Act, § 126, 11 U.S.C. § 526 (1970). An involuntary petition may be filed either by three or more creditors holding certain specified claims or by an indenture trustee. *Id.*

²² The court will dismiss the petition unless it is satisfied that it has been filed in good faith and complies with the statutory requirements. *Id.*, § 141, 11 U.S.C. § 541 (1970). All petitions are required to include certain information. *Id.*, § 130, 11 U.S.C. § 530 (1970). Additional information must be included in petitions filed by creditors or indenture trustees. *Id.*, § 131, 11 U.S.C. § 531 (1970).

²³ Bankruptcy Act, § 265(a), 11 U.S.C. § 665(a) (1970). Other specific sections which require notice to the Commission, whether or not it decides to file an appearance, include: *id.*, § 161, 11 U.S.C. § 561 (1970) (hearing on the approval of the petition); *id.*, § 167(5), 11 U.S.C. § 567(5) (1970) (report of trustee's investigation of the debtor); *id.*, § 171, 11 U.S.C. § 571 (1970) (hearing on the plan); *id.*, § 229(b), 11 U.S.C. § 629(b) (1970) (application for an order declaring consummation of the plan); *id.*, § 247, 11 U.S.C. § 647 (1970) (hearing on application for allowances).

²⁴ *Id.*, § 208, 11 U.S.C. § 608 (1970). The Commission's requests to participate "have been granted almost without exception." 2 Loss, *supra* note 5, at 757.

²⁵ 40 SEC ANN. REP. 123 (1974).

²⁶ *Id.*

²⁷ Bankruptcy Act, § 208, 11 U.S.C. § 608 (1970). ("The Securities and Exchange Commission shall, if requested by the judge, and may, upon its own motion if approved by the judge, file a notice of its appearance in a proceeding under this chapter.")

²⁸ Bankruptcy Act, § 208, 11 U.S.C. § 608 (1970).

various issues which arise in the proceeding. In addition, the SEC participates regularly in informal conferences and discussions with the parties. The Commission views its informal participation as having at least equal importance as its more formal appearances in fulfilling its function of protecting public investors.²⁹ The only limitations on the Commission's status as a party in interest are that it has no right to appeal³⁰ and no right to claim compensation from the debtor's estate.³¹ Denial of appellate standing, however, does not prevent the Commission from joining, as a party or *amicus curiae*, in appeals filed by other participants in the proceedings.³² In addition, the SEC may also seek mandamus in order to vindicate its position in appropriate cases.³³ Section 208, therefore, gives the SEC "participation rights similar to those of other parties in a chapter X proceeding"³⁴ except insofar as it denies the Commission the right to appeal.

B. Administration of the Debtor's Estate

After the court has approved the petition,³⁵ the judge will appoint a "disinterested" trustee if the corporation's indebtedness exceeds a specified amount;³⁶ otherwise, the debtor may continue in possession.³⁷ Both the trustee and the debtor in possession are court officers³⁸ who have primary responsibility for administering the

²⁹ 10 SEC ANN. REP. 144 (1944).

³⁰ Bankruptcy Act, § 208, 11 U.S.C. § 608 (1970). See Windle, *The Securities and Exchange Commission and Corporate Reorganizations under Chapter X*, 34 REF. J. 37 (1960) [hereinafter cited as Windle]. There is no legislative history explaining the congressional intent in preventing the SEC from initiating an appeal. SEC REPORT ON PROPOSED LEGISLATION, *supra* note 5, at 13. The Commission, however, speculates that Congress felt that a government agency should not be allowed to delay the proceeding by taking an appeal when none of the parties with an economic interest in the court's order had chosen to do so. *Id.* Nevertheless, it has been suggested that affording the Commission a right to appeal would increase its effectiveness. Windle, *supra* at 43.

³¹ Bankruptcy Act, § 242, 11 U.S.C. § 642 (1970).

³² See, e.g., *In re Imperial "400" Nat'l, Inc.*, 432 F.2d 232, 234 (3d Cir. 1970); *In re American Nat'l Trust*, 426 F.2d 1059, 1066 (7th Cir. 1970); *Ashbach v. Kirtley*, 289 F.2d 159, 162 (8th Cir. 1961); 2 LOSS, *supra* note 5, at 756.

³³ SEC v. Krentzman, 397 F.2d 55, 59 (5th Cir. 1968). The Commission had been denied the right to cross examine witnesses and offer evidence by the district court. In granting the SEC's requested writ, the court of appeals noted that in the context of a denial of the Commission's right to participate effectively in the proceedings: "The absence of review at the behest of the Commission makes all the more appropriate a writ to enable it to perform its task." *Id.* But see SEC v. Templar, 405 F.2d 126, 128 (10th Cir. 1969) (denying writ of mandamus sought by SEC where none of the stockholders whom the SEC sought to protect had raised timely claims).

³⁴ SEC v. Templar, 405 F.2d 126, 128 (10th Cir. 1969) (footnote omitted).

³⁵ See note 22 *supra*.

³⁶ Bankruptcy Act, § 156, 11 U.S.C. § 556 (1970) (appointment of a trustee is mandatory when "the indebtedness of a debtor, liquidated as to amount and not contingent as to liability, is \$250,000 or over . . .")

³⁷ *Id.*

³⁸ Bankruptcy Act, §§ 186-89, 11 U.S.C. §§ 586-89 (1970).

debtor's estate³⁹ and for formulating the plan of reorganization for submission to the court.⁴⁰ As court officers, their titles, rights and powers derive from the extensive authority enjoyed by the court in the administration of the debtor's estate during the reorganization proceedings. The court, for example, exercises plenary jurisdiction over actions brought by the trustee or debtor in possession against third persons on claims belonging to the estate.⁴¹ Furthermore, as a court of equity, it has summary jurisdiction to protect the *res* within its control.⁴² Accordingly, the statute specifically confers upon the court the authority to enjoin or stay suits,⁴³ to permit the trustee to reject executory contracts of the debtor,⁴⁴ to authorize him to issue certificates of indebtedness⁴⁵ and to lease or sell any of the debtor's property.⁴⁶ With respect to these administrative matters, the SEC's participation in the proceedings has tended to focus on three central concerns: the qualification and performance of fiduciaries, the jurisdiction of the court to take certain actions, and the sale of substantial assets of the debtor.

1. Scrutiny of the Qualification and Performance of Fiduciaries.

The Commission is particularly active in scrutinizing the qualifi-

³⁹ *Id.*, § 189, 11 U.S.C. § 589 (1970).

Because a debtor continued in possession "shall have all the title, be vested with all the rights, be subject to all the duties, and exercise all the powers of a trustee appointed under this chapter," Bankruptcy Act, § 188, 11 U.S.C. § 588 (1970), the SEC's role, whether or not the debtor continues in possession, is substantially the same. One distinction, however, is that the continuation of the debtor in possession obviates the need to scrutinize the "disinterested" status of a trustee who otherwise might have been appointed. Nevertheless, it would authorize the SEC to object to the retention of the debtor in possession upon the ground that he is not qualified or is not disinterested. *Id.*, § 162, 11 U.S.C. § 562 (1970). A second distinction stems from the fact that the retention of the debtor in possession indicates that the debtor's liabilities are less extensive such that the Commission, as a practical matter, may be less likely to exercise its discretionary power to intervene because the public holdings are not as large. See text *infra* at notes 47-53. The marked contrast in the procedures of Chapter X and Chapter XI ensures that the Commission's role in a Chapter X case in which the debtor continues in possession is not simply analogous to its participation in a Chapter X case where the debtor *generally* remains in possession. See note 147 *infra*. For a discussion of the contrast between Chapters X and XI, see text & notes *infra* at 143-58 and at 173-77. Thus, it is the character of the proceedings, rather than the simple fact that the debtor continues in possession, which governs the nature of the Commission's role.

⁴⁰ Bankruptcy Act, §§ 167, 169, 11 U.S.C. §§ 567, 569 (1970). If, however, the debtor is continued in possession, the plan may be filed by the debtor, by any creditor or indenture trustee, by a stockholder, if the debtor is not insolvent, or by an examiner appointed by the judge. *Id.*, § 170, 11 U.S.C. § 570 (1970).

⁴¹ See Bankruptcy Act, §§ 2a(6), 2a(7), 102, 11 U.S.C. §§ 11a(6), 11a(7), 502 (1970); 6 COLLIER, *supra* note 4, ¶ 3.18 at 537.

⁴² Bankruptcy Act, § 114, 11 U.S.C. § 514 (1970).

⁴³ *Id.*, § 116(4), 11 U.S.C. § 516(4) (1970). See 6 COLLIER, *supra* note 4, ¶ 3.05 at 429-30.

⁴⁴ Bankruptcy Act, § 116(1), 11 U.S.C. § 516(1) (1970).

⁴⁵ *Id.*, § 116(2), 11 U.S.C. § 516(2) (1970).

⁴⁶ *Id.*, § 116(3), 11 U.S.C. § 516(3) (1970).

cations of persons assuming fiduciary obligations under Chapter X. The statute, for example, specifically requires that the trustee⁴⁷ and the attorney appointed to represent him shall be "disinterested"⁴⁸ and defines the circumstances in which a person shall not be deemed to meet the statutory standard.⁴⁹ These provisions are designed to ensure that the court's appointees be "free of connections not only with the old management but with all of its associates" in order to effectuate the ultimate purpose of securing "independent and faithful administration of distressed properties."⁵⁰ Therefore, when confronted with evidence of even a possible conflict of interest,⁵¹ the Commission will urge that the fiduciary voluntarily resign.⁵² If the fiduciary refuses to resign, the SEC may file a formal objection to his appointment thus requiring the court to rule on his qualification.⁵³ In *Calvin Christan Retirement Home, Inc. v. Paire, Inc.*,⁵⁴ for example, the SEC petitioned for a disqualification of the attorney appointed as general counsel for the trustee on the ground that he was not disinterested since he concurrently represented the creditors who had petitioned for an involuntary reorganization of the debtor.⁵⁵ The Commission, then, generally seeks to ensure that persons employed as trustees and attorneys in the course of Chapter X proceedings meet the statutory standard of "disinterest" which was considered one of the central aims of that chapter.⁵⁶

⁴⁷ *Id.*, § 156, 11 U.S.C. § 556 (1970).

⁴⁸ *Id.*, § 157, 11 U.S.C. § 557 (1970).

⁴⁹ Chapter X specifies the standards of disinterestedness which apply to the trustee and his attorney. *Id.*, § 158, 11 U.S.C. § 558 (1970). In addition to proscribing the appointment of persons standing in certain specified relationships to the debtor, such as creditor, stockholder, underwriter of any of its outstanding securities, director, officer, or employee, the section includes the flexible catchall disqualification for persons having "for any reason an interest materially adverse to the interests of any class of creditors or stockholders," *Id.*, subsection (4). Against these statutory tests, the personal integrity or ability of a person is immaterial. 6 COLLIER, *supra* note 4, ¶ 7.03 at 1163.

⁵⁰ Teton, *Reorganization Revised*, 48 YALE L.J. 573, 574 (1939).

⁵¹ The statutory tests of disinterestedness are strictly applied. See 6 COLLIER, *supra* note 4, ¶ 7.03 at 1162-63; Windle, *supra* note 30, at 41.

⁵² See, e.g., *In re Congaree Iron & Steel Co.* (D.S.C. No. 72-72) and *In re Tilco, Inc.* (D. Kan., No. 23662), reported in 39 SEC ANN. REP. 118 (1973).

⁵³ The court has the power "at any time, without or upon cause shown" to remove trustees and appoint substitute trustees. Bankruptcy Act, § 160, 11 U.S.C. § 560 (1970). Hearings on objections to the retention of a trustee in office are mandatory. *Id.*, §§ 160, 161, 11 U.S.C. §§ 560, 561 (1960).

⁵⁴ (W.D. Mich., Nos. G-74-1113-B-1 & G-74-1114-B-1), reported in 41 SEC ANN. REP. 151 (1975).

⁵⁵ As a result of the Commission's petition, the order finding the attorney disinterested and appointing him as general counsel to the trustee was withdrawn. Thereafter, a new general counsel was appointed. *Id.* See *Tilco, Inc.*, (D. Kan., No. 23662), reported in 39 SEC ANN. REP. 118 (1973). In *Tilco*, a lawyer, appointed by the court as general counsel to the trustee, resigned when advised by the SEC that he was not disinterested because he had been associated with the law firm which acted as counsel for the debtor within two years preceding the filing of the Chapter X petition. *Id.*

⁵⁶ The mandatory appointment of a disinterested trustee in certain cases has been termed the "keystone" to the reforms effectuated by the Chandler Act. Teton,

Just as the Commission seeks to oversee the disinterested character of trustees and their attorneys, it also has been active in monitoring the fiduciary status⁵⁷ of corporate officers and committees representing creditors or stockholders and will challenge their failure to comply with the statutory authorization process.⁵⁸ The SEC will oppose efforts by unauthorized individuals to solicit funds from public investors for the ostensible purpose of organizing and representing protective committees.⁵⁹ Similarly, the Commission will seek the disqualification of committees subject to possible conflicts of interest. Accordingly, it may oppose committees seeking to represent different classes of creditors or stockholders or committees composed of former insiders who have been charged with mismanagement.⁶⁰ When a committee, however, is duly authorized under the statute, the Commission will support it in its battle to retain representative status.⁶¹ In

Reorganization Revised, 48 YALE L. J. 573, 574 (1939). Significantly, in its reports which were an important factor prompting the enactment of the Chandler Act, the SEC devoted considerable attention to the problems created by the presence of conflicts of interest in corporate reorganizations. See SEC PROTECTIVE COMMITTEE STUDY, *supra* note 5, Part I, at 355-57; Part II, at 164-294.

⁵⁷ *Woods v. City Nat'l Bank & Trust Co.*, 312 U.S. 262, 268 (1941) (recognizing the fiduciary status of committees and others representing creditors and stockholders).

⁵⁸ Section 209 authorizes any creditor or stockholder to "act in person, by an attorney at law, or by a duly authorized agent or committee." Bankruptcy Act, § 209, 11 U.S.C. § 609 (1970). Section 211 requires each such representative committee to file with the court a statement which includes a statement of the terms of its employment, a copy of the instrument empowering them to act on behalf of creditors or stockholders and a showing of the claims or stock represented by such committee. *Id.*, § 211, 11 U.S.C. § 611 (1970). Section 210, 11 U.S.C. § 610 (1970) requires an attorney for creditors or stockholders to file a similar statement. The right of appearance of every person or committee, representing more than twelve creditors, and every indenture trustee, is conditioned on the filing of this statement. 6A COLLIER, *supra* note 4, ¶ 9.30 at 345. These committees and representatives are subject to the court's regulation and control. Bankruptcy Act, § 212, 11 U.S.C. § 612 (1970). Furthermore, committees purporting to represent creditors or stockholders may not be heard in the proceedings until they have complied with all other applicable laws, including the federal securities laws. *Id.*, § 213, 11 U.S.C. § 613 (1970); *In re First Home Investment Corp.*, 368 F. Supp. 597, 602 (D. Kan. 1973).

⁵⁹ *In re First Home Investment Corp.*, 368 F. Supp. 597, 599 (D. Kan. 1973). In that case, the Commission obtained a court order enjoining a former officer and director of the debtor from further solicitations for representative status. Furthermore, the SEC also moved the court to order the former officer to account for all receipts and disbursements. *Id.* at 603. Once the accounting was filed the Commission promptly objected to it and requested disallowance of all claimed expenses. 40 SEC ANN. REP. 125 (1974). See also Imperial-American Resources Fund, Inc., (D. Colo., No. 72-B-556), reported in 39 SEC ANN. REP. 119 (1973), where the district court, on application of the Commission, ordered an individual to cease soliciting funds and representative authority from certain limited partnerships in which the debtor was a general partner because he had not complied with the applicable provisions of Chapter X.

⁶⁰ Windle, *supra* note 30, at 42.

⁶¹ *Cf. American Nat'l Trust v. Shanklin*, 420 F.2d 1117, 1118-19 (7th Cir. 1970), cert. denied, 400 U.S. 823 (1971), *reh'g denied*, 404 U.S. 979 (1971), where the court affirmed a district court order dismissing a motion by a certificate holder of the debtor trusts to vacate the orders approving the reorganization petitions filed by other certificate holders. The motion had questioned the standing of the certificate holders. How-

Protective Committee v. Kirkland,⁶² for example, the SEC supported the common stockholder committee's appeal of a lower court order requiring the committee to file new authorizations from the stockholders. Ruling in its favor, the Fifth Circuit stated that it was "unwilling to see the role of the Committee downgraded or impeded by the court's order and agree[d] with the SEC that the order [was] without adequate justification."⁶³ Thus, the SEC will oversee the fiduciary status of committees, and may either challenge their failure to observe the statutory authorization process, or may support their compliance therewith, whether on its own motion or on motions brought by other parties in interest.

Once it has scrutinized the qualification of fiduciaries, the SEC also may assist them in the performance of their duties. In particular, the Commission staff regularly aids the trustee both in his investigation of the debtor and in his compliance with statutory reporting requirements.⁶⁴ This accounting of corporate affairs is one of the trustee's primary duties in Chapter X proceedings and it stems from two distinct but overlapping sources. Section 167(1), as augmented by section 167(3), requires the trustee, when so directed by the court, to report to the judge on the "acts, conduct, property, liabilities, and financial condition of the debtor,"⁶⁵ as well as to communicate "any facts . . . pertaining to fraud, misconduct, mismanagement and irregularities, and to any causes of action available to the estate."⁶⁶ The assistance rendered by the SEC in the course of this investigation takes many forms. Initially, it may urge the court to direct the trustee to conduct the investigation once the reorganization court has taken jurisdiction.⁶⁷ Thereafter the Commission's investigation may disclose misconduct by persons connected with the debtor which otherwise might not have been uncovered.⁶⁸ In addition to uncovering such

ever, the court held that the orders approving the petitions had become final and that objections should have been raised at the hearing at which the court first approved the petition.

⁶² 481 F.2d 606, 607 (5th Cir. 1973) (per curiam).

⁶³ *Id.* at 607.

⁶⁴ 38 SEC ANN. REP. 118 (1972).

⁶⁵ Bankruptcy Act, § 167(1), 11 U.S.C. § 567(1) (1970).

⁶⁶ *Id.*, § 167(3), 11 U.S.C. § 567(3) (1970).

⁶⁷ See *In re Federal Coal Co.*, 335 F. Supp. 1183, 1185 (S.D. W. Va. 1971).

⁶⁸ See *Windle*, *supra* note 30, at 38. The Commission may participate in the examination of witnesses. See *In re Commonwealth Fin. Corp.*, 408 F.2d 640, 641 (3d Cir.) (per curiam), *cert. denied*, 395 U.S. 961 (1969). The SEC is most active in cases presenting alleged violations of the federal securities laws. See 40 SEC ANN. REP. 126-27 (1974). An investigative report by the SEC may reveal the presence of insider trading upon which the trustee can sue for a direct return of short-swing profits to the corporation. *In re R. Hoe & Co.* (S.D.N.Y., No. 69-B-461, 1969), *reported in* 40 SEC ANN. REP. 126 (1974). An SEC-aided trustee's investigation may provide sufficient data for private plaintiffs to bring either individual or class action suits against officers, directors or professional advisors, such as accountants, for contravention of federal securities laws. *In re Dolly Madison Indus., Inc.* (E.D. Pa. 1970), *reported in* 39 SEC ANN. REP. 126 (1973).

causes of action, the SEC will notify the court of any failure on the part of the trustee to pursue them.⁶⁹ Furthermore, once the trustee takes action and begins to negotiate with the alleged malfasants or to compromise other claims, the Commission will scrutinize any proposed settlement agreements especially where the alleged violations involve the federal securities laws.⁷⁰ Thus, the Commission may urge the court confronted with such a compromise agreement to "hold a hearing so that evidence can be presented to permit a fair assessment of the compromise."⁷¹

Not only does the SEC assist the trustee in investigating the debt- or pursuant to the request of the judge under section 167(1), but it may also become involved in enforcing the requirement of section 167(5) that the trustee file reports on the continued management of the debtor's estate.⁷² Unlike the investigation under section 167(1) which is made only upon the order of the judge and which seeks in particular to uncover fraud or misconduct in the debtor's affairs which might give rise to claims against the estate, the periodic reports made under section 167(5) are mandatory and their subject matter—the financial condition of the debtor—is more restricted in scope.⁷³ Although the statute fails to specify an established form for these reports, minimally they should contain "[a] periodic balance sheet and profit-and-loss statement. . . ; statements of bank deposits . . . ; [separate statements of] the financial condition of subsidiaries. . . ; and annual reports"⁷⁴

The SEC's involvement in the trustee's compliance with these investigation and reporting requirements imposed by the bankruptcy laws is particularly appropriate in view of the fact that these requirements effectively parallel the investigation and reporting provisions of the federal securities laws. The Securities Acts require the SEC to in-

⁶⁹ *Committee v. Kent*, 143 F.2d 684, 686 (4th Cir. 1944) (per curiam).

⁷⁰ See *Arlan's Dept. Store, Inc.*, (S.D.N.Y., No. 73-B-468), reported in 41 SEC ANN. REP. 153 (1975), where the court approved, over the objection of the SEC, a cash settlement of a shareholder's derivative action against the debtor's management. Since the trustee had not had the opportunity to conduct the required investigation, the Commission urged that the investigation be made so that the trustee could then present facts from which an informed judgment could be reached on the adequacy of the settlement figure. The SEC had contended that the cash figure was not so significant in light of the debtors' needs to warrant relinquishing possible claims. *Id.*

⁷¹ 40 SEC ANN. REP. 127 (1974), citing *In re R. Hoe & Co., Inc.* (S.D.N.Y., No. 69-B-461, 1969). See also *In re Westec Corp.* (S.D. Texas, No. 66-H-62, 1966) reported in 40 SEC ANN. REP. 126 (1974).

⁷² Bankruptcy Act, § 167(5), 11 U.S.C. § 567 (5) (1970); Ch. X R. 10-208; Corotto, *SEC Reporting, Proxy and Antifraud Compliance—An Additional Perspective on Bankruptcy Reorganization Proceedings*, 63 CAL. L. REV. 1563, 1572 (1975) [hereinafter cited as Corotto]. The Bankruptcy Rules specifically provide that "[t]he Securities and Exchange Commission may recommend the form of such reports and summaries." Ch. X R. 10-208(c). Furthermore, copies of the trustee's report filed under § 167(5) must be submitted to the SEC. Bankruptcy Act, § 167(5), 11 U.S.C. § 567(5) (1970).

⁷³ See 6 COLLIER, *supra* note 4, ¶ 7.22 at 1233-34.

⁷⁴ Corotto, *supra* note 72, at 1572.

investigate any actual or threatened violations of their provisions.⁷⁵ The scope of such an investigation clearly overlaps with an investigation conducted by the trustee under section 167(1) of the Bankruptcy Act to the extent that both "contemplate to some extent, the devolution of fraudulent practices by persons in control and operation of the debtor corporation."⁷⁶ Similarly, the registered reporting status of a corporate debtor⁷⁷ requires it to disclose information to the SEC⁷⁸ which is very similar in character to that which the trustee must submit to the court under section 167(5) of the Bankruptcy Act.⁷⁹ As a result of this overlap, the SEC may already have received or gathered much information pertinent to a corporate reorganization and therefore may readily assist the trustee or ensure his compliance with his statutory duties under the Bankruptcy Act.

2. Activities on Behalf of the Jurisdiction of the Court.

In addition to the performance and qualification of fiduciaries, a second major concern of the Commission's participation in Chapter X proceedings has been to thwart attempts to interfere with the exclusive jurisdiction of the reorganization court. A reorganization court has exclusive jurisdiction of the property of the debtor, wherever located,⁸⁰ and may enjoin or stay "the commencement or continuation of a suit against a debtor."⁸¹ Bankruptcy courts are "essentially courts of equity" and have "the power to issue an injunction when necessary to prevent the defeat or impairment of [their] jurisdiction."⁸² In rec-

⁷⁵ Securities Act of 1933, § 20(a), 15 U.S.C. § 77(t) (1970); Securities Exchange Act of 1934, § 21(a), 15 U.S.C. § 78u(a) (1970). The Commission would be derelict in failing so to investigate. *United States v. Parrott*, 315 F. Supp. 1012, 1015 (S.D.N.Y. 1969), *aff'd*, 425 F.2d 972 (2d Cir. 1970), *cert. denied*, 400 U.S. 824 (1970).

⁷⁶ *In re Commonwealth Fin. Corp.*, 288 F. Supp. 786, 788 (E.D. Pa. 1968), *aff'd per curiam*, 408 F.2d 640 (3d Cir. 1969), *cert. denied*, 395 U.S. 961 (1969) (footnote omitted).

⁷⁷ Securities issued by the debtor corporation may have been registered under § 12(b) of the Securities and Exchange Act of 1934, 15 U.S.C. § 781(b) (1970) (when traded on a national securities exchange); under § 12(g) of the Securities and Exchange Act of 1934, 15 U.S.C. § 781(g) (1970) (when engaged in interstate commerce or whose securities are traded by means of the mails or by an instrumentality of interstate commerce and which has total assets exceeding \$1,000,000); or may have been issued by a registered offering under § 5 of the Securities Act of 1933, 15 U.S.C. § 77(e) (1970).

⁷⁸ Section 13(a) of the Securities Exchange Act of 1934, 15 U.S.C. § 17m(a) (1970).

⁷⁹ The information required is that which ensures that previously filed registrations are "reasonably current" and therefore includes transactions leading to changes in the control of the registrant; acquisitions or dispositions of assets; legal actions; changes in securities, or in amounts of securities outstanding; financial statements, etc. SEC Form 8-K in PRACTICING LAW INSTITUTE, SECURITIES REGULATION SOURCEBOOK 7-83 (R.L. Krauss ed. 1972-73). See generally Corotto, *supra* note 72, at 1571-76, 1605-08.

⁸⁰ Bankruptcy Act, § 111, 11 U.S.C. § 511 (1970).

⁸¹ *Id.*, § 113, 11 U.S.C. § 513 (1970).

⁸² *In re Imperial "400" Nat'l Corp.*, 429 F.2d 680, 682 (3d Cir. 1970) (*per curiam*), quoting *Continental Ill. Nat'l Bank & Trust Co. v. Chicago Rock Island & Pac. Ry.*, 294 U.S. 648, 675 (1935).

ognition of the increasingly liberal interpretations courts have given to the scope of the reorganization court's authority,⁸³ the SEC often will appear in support of the court's jurisdiction to take whatever actions are necessary to effectuate the rehabilitation of the debtor. Thus, in *In Re Imperial "400" National, Inc.*,⁸⁴ the Commission appeared in support of the lower court's order, affirmed on appeal,⁸⁵ which enjoined further prosecution in another court of an ordinary bankruptcy proceeding involving a partnership in which the debtor corporation was a partner.⁸⁶ Similarly, in *In re Traders Compress Co.*,⁸⁷ the SEC joined with the trustees of a corporate propane gas distributor undergoing reorganization in seeking an injunction restraining the gas supplier from terminating its supply contract.⁸⁸ Notwithstanding that the supply agreement gave the supplier the right to terminate the contract, the district court held that it had jurisdiction to issue a permanent injunction to delay the enforcement of the contract in order to effect the reorganization of the distributor.⁸⁹ The SEC, then, generally appears in order to uphold the jurisdiction of the court where necessary to accomplish the debtor's reorganization. To the extent, however, that the SEC considers that the court's exercise of that jurisdiction will conflict with the ultimate purpose of corporate rehabilitation, it may oppose the proposed action on the merits.

3. Lease or Sale of Substantial Assets of the Debtor.

One primary area of administration in which the SEC consistently has opposed court-authorized proposed action on the merits involves the lease or sale of the debtor's property. Section 116(3) enables the judge, upon the approval of a petition, to "authorize a re-

⁸³ See *In re Internat'l Power Sec. Corp.*, 170 F.2d 399, 402 (3d Cir. 1948). See also *Continental Ill. Nat'l Bank & Trust Co. v. Chicago Rock Island & Pac. Ry.*, 294 U.S. 648, 675-76 (1935).

⁸⁴ 429 F.2d 671 (3d Cir. 1970), noted in 36 SEC ANN. REP. 176-77 (1970).

⁸⁵ *Id.* at 679.

⁸⁶ Appellants contended that the bankruptcy court's exclusive jurisdiction over the "property" of the debtor extends only to the kind of property for which title passes to the trustee upon appointment. *Id.* at 678. Therefore, they concluded that the court has no jurisdiction to enjoin the ordinary bankruptcy proceeding because the debtor, holding only a 75% interest in the partnership, did not have such title to the assets of the partnership. *Id.* The court, however, determined that the term "property" in § 111 of the Bankruptcy Act, 11 U.S.C. § 511 (1970), must be construed "most generously" and does not depend on traditional concepts. 429 F.2d at 678. Therefore, the court concluded that the lower court had jurisdiction to enjoin the bankruptcy proceeding where the partnership involved was an integral part of the debtor's business operation whose liquidation clearly would affect the latter's reorganization. *Id.* at 677-79. See *In re Equity Funding Corp.*, 396 F. Supp. 1266, 1273-74 (C.D. Cal. 1975) (SEC supports position of trustee who had filed application to enjoin prosecution of certain fraud claims against subsidiaries of the debtor which had filed a petition for reorganization. The court upheld its jurisdiction to issue the injunction).

⁸⁷ 381 F. Supp. 789 (W.D. Okla. 1973) (mem.).

⁸⁸ *Id.* at 791.

⁸⁹ *Id.* at 793.

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ceiver or a trustee or a debtor in possession, upon such notice as the judge may prescribe and upon cause shown, to lease or sell any property of the debtor, whether real or personal, upon such terms and conditions as the judge may approve."⁹⁰ The complexities of corporate business have made the need to "prune a debtor's business" in order to facilitate its reorganization an almost "routine aspect" of Chapter X administration.⁹¹ While the Commission recognizes the need to avoid freezing the debtor in the same position which caused its insolvency,⁹² it nevertheless subjects sales of major assets of the debtor, pursuant to section 116(3), to close scrutiny because these sales may lead to the liquidation of the debtor without a vote by security holders and may thereby reduce the plan of reorganization to the ratification of a fait accompli.⁹³ Accordingly, the Commission has adopted a presumption against proposed sales of all or a critical portion of a debtor's assets under the summary procedure of section 116(3) and will support them only in "exceptional circumstances."⁹⁴ In the absence of the requisite "exceptional circumstances," the Commission's opposition to the sale may take various forms. It may oppose the sale outright.⁹⁵ Alternatively, it may agree with the basic decision to sell, but may predicate its support on the court's disposition of secondary factors. For example, the SEC may take the position that the offer being considered is inadequate.⁹⁶ Similarly, it

⁹⁰ 11 U.S.C. § 516(3) (1970).

⁹¹ 39 SEC ANN. REP. 120 (1973). In addition to noting the "increasing complexities" of corporations, the SEC expressly faulted "the indiscriminate diversification which may precede corporate failures" *Id.*

⁹² *Id.*

⁹³ See 39 SEC ANN. REP. 120 (1973); 38 SEC ANN. REP. 115-16 (1972). The summary procedure of § 116(3) should be contrasted with § 216(10), dealing with plans of reorganization, which expressly allows the plan to provide for the sale of any or all of the debtor's assets. 11 U.S.C. § 616(10) (1970). A sale pursuant to a plan of reorganization under § 216(10) is not committed to the court's sole discretion, but requires compliance with the statutory protective devices surrounding the adoption of the plan. A sale in the latter case, therefore, must be approved by a majority of creditors and stockholders who are the beneficial owners of the property in question. 39 SEC ANN. REP. 120 (1973).

⁹⁴ 39 SEC ANN. REP. 120 (1973); 38 SEC ANN. REP. 115-16 (1972). "Exceptional circumstances" authorizing a sale, however, are not limited to emergencies or situations where there is imminent danger of loss to the corporation. *In re Equity Funding Corp.*, 492 F.2d 793, 794 (9th Cir.) (per curiam), cert. denied, 419 U.S. 964 (1974). In that case, the court affirmed the bankruptcy court's order authorizing the debtor's trustee, as sole stockholder of a wholly owned subsidiary of the debtor, to consent to a sale of assets of subsidiary. *Id.* The court determined that the trial court could properly have concluded that there was "cause shown" for the approval of the sale on the basis of findings of fact that the market value of the subsidiary was likely to decline substantially in the near future. *Id.*

⁹⁵ *In re Solar Mfg. Corp.*, 176 F.2d 493, 494 (3d Cir. 1949), *aff'd in part, rev'd in part on other grounds*, 190 F.2d 273 (1951), cert. denied, 342 U.S. 893 (1951); *Bubble Up Del., Inc.* (C.D. Cal., Nos. 78641-FW, 78950-FW, 79596-FW, and 80470-FW), reported in 39 SEC ANN. REP. 121 (1973).

⁹⁶ *In re Bernec Corp.* (S.D.N.Y. No. 71-B-291, 1971) reported in 39 SEC ANN. REP. 121 (1973). For a case where the court scrutinized the adequacy of the consideration, see *In re Penn Cent., Transp. Co.*, 356 F. Supp. 285 (E.D. Pa. 1973) (mem.).

may advocate that the court mandate a particular disposition of the sale proceeds.⁹⁷ Furthermore, where different potential purchasers submit bids, the Commission may recommend that the parties submit proposed plans of sale to the trustee; so that the sale would be made pursuant to a plan and therefore would require a vote of the security holders affected by it.⁹⁸ In effect, therefore, with respect to this aspect of the administration of the debtor's estate, the Commission assumes an overseer role whereby it seeks to avoid the expansion of a fiduciary's authority in a manner which it views as potentially conflicting with the very philosophy of reorganization.⁹⁹

C. Plan of Reorganization

Although the SEC is actively concerned with the administration of the debtor's estate, the statute, aside from the notice provisions, only mandates its participation in conjunction with the formulation and confirmation of a successful plan whose consummation is the "focal point of the reorganization process."¹⁰⁰ While the trustee has the primary responsibility for the preparation of a plan,¹⁰¹ and the judge has sole responsibility for its ultimate approval,¹⁰² Chapter X institutionalizes the potential for SEC participation at every step of the process.¹⁰³ The SEC's involvement will be most extensive in cases in

⁹⁷ In *In re Equity Funding Corp.*, for example, the SEC's support of the trustee's decision to sell the subsidiary was partially conditioned on the court's requiring the sale proceeds to be deposited in an interest-bearing account from which no withdrawal could be made without approval of the court after notice to interested parties. *In re Equity Funding Corp.* (C.D. Cal., No. 73-03467, 1973), reported in 40 SEC ANN. REP. 125 (1974), *aff'd*, 492 F.2d 793, 794 (9th Cir.) (per curiam), *cert. denied*, 419 U.S. 964 (1974).

⁹⁸ *Bubble Up Del., Inc.* (C.D. Cal., Nos. 78641-FW, 78950-FW, 795960-FW and 80470-FW), reported in 38 SEC ANN. REP. 115 (1972).

⁹⁹ See 39 SEC ANN. REP. 120 (1973).

¹⁰⁰ Windle, *supra* note 30, at 39.

¹⁰¹ Bankruptcy Act, §§ 167, 169, 11 U.S.C. §§ 567, 569 (1970). If, however, the debtor is continued in possession, the plan may be filed by the debtor; by any creditor or indenture trustee; by a stockholder, if the debtor is not insolvent; or by an examiner appointed by the judge. *Id.*, § 170, 11 U.S.C. § 570 (1970).

¹⁰² 6 COLLIER, *supra* note 4, ¶7.30 at 1263. The judge's approval of a plan is conditioned on his finding that the plan complies with § 216, 11 U.S.C. § 616 (1970), and is "fair and equitable, and feasible." Bankruptcy Act, § 174, 11 U.S.C. § 574 (1970). Section 221, 11 U.S.C. § 621 (1970), governs the court's confirmation of a plan.

¹⁰³ After appointment of the trustee, the judge will fix a time for a hearing on the plan. Bankruptcy Act, §§ 169, 170, 11 U.S.C. §§ 569, 570 (1970). Notice of the time of this hearing must be given to the Commission. *Id.*, § 171, 11 U.S.C. § 571 (1970). After the hearing and before approval of the plan, the judge may submit the plan to the SEC for report if the scheduled indebtedness is less than \$3,000,000, and must do so where the scheduled indebtedness exceeds \$3,000,000. *Id.*, § 172, 11 U.S.C. § 572 (1970). The judge may not approve a plan submitted to the SEC until it has filed a report. *Id.*, § 173, 11 U.S.C. § 573 (1970). After the judge approves the plan, the trustees submit the plan, together with the Commission's report, to all creditors and stockholders affected by it. *Id.*, § 175, 11 U.S.C. § 575 (1970). After the plan has been accepted by a specified percentage of the debtor's creditors, the judge fixes a hearing for consideration of the confirmation of the plan and must notify the SEC. *Id.*, § 179, 11 U.S.C. §

which it files a formal report on the plan. If the corporation's scheduled indebtedness exceeds \$3,000,000, the court must submit the proposed plan to the Commission for an advisory report; the judge *may* submit the plan to the SEC where the scheduled indebtedness is less than \$3,000,000.¹⁰⁴ In such a situation, however, the Commission is likely to file a formal advisory report "only in a case which involves substantial public investor interest and presents significant problems."¹⁰⁵ This report, while merely advisory,¹⁰⁶ often has considerable influence on the eventual acceptance or rejection of a plan.¹⁰⁷

Yet, even in cases where no formal report is filed, the SEC becomes involved as the court and other parties to the proceeding seek to draw on its expertise. The person charged with responsibility for preparing the plan may engage the Commission's assistance in its formulation.¹⁰⁸ Similarly, the SEC will often advise the court of its opinion by letter or may authorize its counsel to present its views orally or in written memoranda.¹⁰⁹

In making either formal or informal reports on reorganization plans, the Commission has given particular attention to the valuation of the debtor's assets. Valuation is the starting point for the determination of the fairness, equity and feasibility of any proposed plan. In *Consolidated Rock Products Co. v. DuBois*, the Supreme Court approved the capitalization of earnings valuation technique there recommended by the SEC.¹¹⁰ Although the SEC generally continues to adhere to the capitalization of earnings approach, it may vary its recommendations in particular cases.¹¹¹ Despite recent criticism of

579 (1970). Similarly hearings on modifications of a plan also require notice to the Commission. *Id.*, § 222, 11 U.S.C. § 622 (1970).

¹⁰⁴ *Id.*, § 172, 11 U.S.C. § 572 (1970).

¹⁰⁵ 40 SEC ANN. REP. 127 (1974). The statute clearly contemplates that the SEC may choose not to file a formal report. See Bankruptcy Act, § 173, 11 U.S.C. § 573 (1970). In practice, the Commission chooses to file such reports in only a small number of cases. In the last five years, for example, it has prepared formal reports only in five cases. 41 SEC ANN. REP. 153 (1975) (none); 40 SEC ANN. REP. 127 (1974) (2); 39 SEC ANN. REP. 123 (1973) (none); 38 SEC ANN. REP. 120 (1972) (3); 37 SEC ANN. REP. 184 (1971) (none).

¹⁰⁶ Bankruptcy Act, § 172, 11 U.S.C. § 572 (1970).

¹⁰⁷ When soliciting the acceptance of a plan on the part of the creditors, the trustee must transmit to them a copy of the SEC's report. *Id.*, § 175, 11 U.S.C. § 575 (1970). See 6 COLLIER, *supra* note 4, ¶ 7.30 at 1263.

¹⁰⁸ See 6 COLLIER, *supra* note 4, ¶ 7.30 at 1264.

¹⁰⁹ 40 SEC ANN. REP. 127 (1974). See 2 LOSS, *supra* note 5, at 756.

¹¹⁰ 312 U.S. 510, 526 (1941). This technique is founded on "the premise that 'value' represents a capitalization of prospective earning power at an appropriate rate which recognizes the risks inherent in the industry and in the particular enterprise." Frank, *Epithetical Jurisprudence and The Work of the Securities and Exchange Commission in the Administration of Chapter X of the Bankruptcy Act*, 18 N.Y.U. L.Q. REV. 316, 341 (1941) [hereinafter cited as Frank].

¹¹¹ Thus, capitalization of estimated net operating profits may be appropriate in one case whereas in another case the proper method may be to discount to present worth the net cash receipts over the life of the enter-

valuation techniques urged by the SEC,¹¹² its approach generally is accorded substantial weight by the court.¹¹³

Beyond providing input on the proper method for the valuation of the debtor's assets, the SEC also attempts to ensure that the court apply appropriate standards in determining the fairness and feasibility of the proposed plan. For the purposes of assessing the fairness of a plan, the Commission consistently has advocated the application of the "absolute priority rule,"¹¹⁴ which posits that a plan is not "fair and equitable" "unless it provides participation for claims and interests in complete recognition of their strict priorities, and unless the value of the debtor's assets supports the extent of the participation afforded each class of claims or interests included in the plan."¹¹⁵ In evaluating the feasibility of a plan, the Commission, therefore, will consider a number of different factors:

whether the total debt is reasonable when compared with the capitalized valuation of the debtor, whether the expected earning power will be sufficient to meet the fixed charges, whether proposed dividends can be paid, whether there are provisions for adequate working capital, the effect of the new capitalization on prospective credit, the adequacy of sinking fund provisions, and whether the proposed capital structure is in conformity with sound business and accounting practice.¹¹⁶

The Commission's assessment of the feasibility of a proposed plan is particularly significant because it is closely related to its duties under the federal securities laws. Because the sale and distribution of securities issued pursuant to a plan of reorganization is exempt¹¹⁷ from the registration requirements of section 5 of the Securities Act

prise. If liquidation value exceeds going-concern value, the Commission has not hesitated to recommend liquidation and the debtor's assets should of course, be valued on a liquidation basis. In a case involving an investment company with readily marketable securities, the Commission valued the assets by reference to market quotations rather than capitalization of prospective earnings.

Windle, *supra* note 30, at 40 (citations omitted).

¹¹² See generally Blum, *Corporate Reorganization Doctrine as Recently Applied by the Securities and Exchange Commission*, 40 U. CHI. L. REV. 96 (1972).

¹¹³ See *Moulded Prods., Inc. v. Barry*, 474 F.2d 220, 225 (8th Cir.) (stressing the importance of this "going concern" valuation), *cert. denied*, 412 U.S. 940 (1973).

¹¹⁴ The Court has characterized the "fair and equitable" standard as incorporating the absolute priority doctrine. *Protective Comm. for Indep. Stockholders of TMT Trailer Ferry, Inc. v. Anderson*, 390 U.S. 414, 441 (1968).

¹¹⁵ 6 COLLIER, *supra* note 4, ¶ 11.06 at 613 (footnote omitted).

¹¹⁶ *Id.*, ¶ 11.07 at 639-40 (footnotes omitted). See *In re Imperial "400" Nat'l, Inc.*, 374 F. Supp. 949, 956, 957-58 (D.N.J. 1974); *SEC v. S & P Nat'l Corp.*, 273 F. Supp. 863, 869 (S.D.N.Y. 1967).

¹¹⁷ Bankruptcy Act, § 264(a), 11 U.S.C. § 664(a) (1970). The exemption is limited, however, and it does not apply to transactions by an issuer or an underwriter in connection with a distribution, otherwise than pursuant to a plan. *Id.*, § 264(a)(2), 11 U.S.C. § 664(a)(2) (1970).

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of 1933,¹¹⁸ the Commission can safeguard the rights of both present security holders and future security purchasers only by insisting on strict compliance with the feasibility requirement which will help prevent the circulation of unsound securities.¹¹⁹ Furthermore, these provisions affording the reorganization court the technical facilities and expert advisory assistance of the SEC are particularly critical because the character of the proceeding as "a complex admixture of legal, business, financial and economic problems" is at no point "more manifest than in the formulation and scrutiny of the reorganization plan itself."¹²⁰ Accordingly, the general consensus is first that the Commission's participation provides the necessary input for making the statutory determination that a plan is "fair and equitable and feasible" and second that its services have been most valuable.¹²¹

D. Compensation

Chapter X provides "detailed machinery"¹²² which governs both claims for costs and expenses incurred in the administration of the debtor's estate as well as claims of compensation for services rendered.¹²³ While the bankruptcy court has exclusive jurisdiction

¹¹⁸ 15 U.S.C. § 77(e) (1970).

¹¹⁹ Note, *The Role of the SEC in Corporate Reorganizations under the Bankruptcy Act*, 1958 ILL. L. FOR. 631, 640-41 (1958). In this connection, the Commission has remarked:

Bankruptcy reorganization . . . is a significant source of entry of new securities into the public trading markets. Under the exemption from registration these securities may not be accompanied by disclosure of fundamental information available for other new issues. For this and other reasons of a technical nature, such as a probable preponderance of sellers immediately after reorganization, the 'after-market' for such securities is particularly sensitive to distortion and disruption. SEC REPORT ON PROPOSED LEGISLATION, *supra* note 5, at 101-02.

To protect security holders, the Commission will insist that securities issued pursuant to a plan be in exchange for the debtor's securities; that the old stock have some intrinsic value; and that the exemption be merely transactional and does not in and of itself create an exempt security. 40 SEC ANN. REP. 129 (1974). See generally Corotto, *Debtor Relief Proceedings Under the Bankruptcy Act and the Securities Act of 1933—The Registration Requirement and Its Implications*, 25 HASTINGS L.J. 389 (1974).

¹²⁰ 6 COLLIER, *supra* note 4, ¶ 7.30 at 1258.

¹²¹ See authorities collected in *Id.* ¶ 7.30 at 1258 n.16.

¹²² 6 COLLIER, *supra* note 4, ¶ 13.02 at 899.

¹²³ The statute vests the judge with the authority to "allow reimbursement for proper costs and expenses incurred by the petitioning creditors and reasonable compensation for services rendered and reimbursement for . . . expenses incurred . . . by" referees, special masters, trustees or other officers and their attorneys, the attorney of the debtor, and the attorney for the petitioning creditors. Bankruptcy Act, § 241, 11 U.S.C. § 641 (1970). Similar awards may be made to indenture trustees, depositaries, reorganization managers, committees or representatives of creditors or stockholders, as well as to "any other parties in interest." *Id.*, § 242, 11 U.S.C. § 642 (1970). Additional provision is made for expenses and compensation for creditors, stockholders and their attorneys in connection with the submission of suggestions or proposals of a plan. *Id.*, § 243, 11 U.S.C. § 643 (1970). See *id.*, §§ 244, 245, 11 U.S.C. §§ 644, 645 (1970) (when petition is filed in pending bankruptcy proceeding); *id.*, §§ 246, 248, 11 U.S.C. §§ 646, 648 (1970) (upon dismissal of proceeding or adjudication of bankruptcy); *id.*, § 249, 11

over all compensation and expenses,¹²⁴ the Commission has played a major role in the court's determination of the propriety and amount of such allowances. Courts commonly will request the SEC to submit its recommendations on the disposition of fee applications.¹²⁵ In response to such requests, the Commission often conducts extensive investigations resulting in detailed reports to the court. The magnitude of the task,¹²⁶ together with the experience¹²⁷ and independence¹²⁸ of the Commission, in practice have insured that the SEC's recommendations will be afforded substantial weight.¹²⁹

The substance of the SEC's recommendations is, in turn, a

U.S.C. § 649 (1970) (requiring statement by persons petitioning for allowances of claims or stock acquired or transferred after commencement of the proceeding). Related provisions affirming judicial control over allowances include: *id.*, §§ 212, 216(3), 221(4), 11 U.S.C. §§ 612, 616(3), 621(4) (1970). The enactment of these provisions was largely a response to extensive criticism of the widespread abuse in the practice of reorganization allowances. See Note, *The SEC and Allowance in Corporate Reorganization*, 42 GEO. L. J. 420, 421 (1954).

¹²⁴ Woods v. City Nat'l Bank & Trust Co., 312 U.S. 262, 267 (1941). See sections of the Bankruptcy Act cited *supra* note 123.

¹²⁵ See, e.g., *In re Inland Gas Corp.*, 193 F. Supp. 62, 64 (E.D. Ky. 1961). SEC Counsel also will participate regularly in the cross-examination of fee applicants during the hearing on the awards. See, e.g., *In re TMT Trailer Ferry, Inc.*, 434 F.2d 804, 807 (5th Cir. 1970) (per curiam), *cert. denied*, 402 U.S. 907 (1971).

¹²⁶ The magnitude of the problem as it may arise in any particular case is exemplified by *In re Yuba Consol. Indus., Inc.*, 260 F. Supp. 930 (N.D. Cal. 1966), where the transcript alone of the hearings on compensation applications occupied 10 volumes with 946 pages of transcript. *Id.* at 933.

¹²⁷ In the last five years, for example, the Commission has reviewed 1547 applications claiming more than a total of \$60 million. 41 SEC ANN. REP. 156 (1975) (411 applications for a total of \$21.1 million); 40 SEC ANN. REP. 130 (1974) (319 applications for a total of \$11 million); 39 SEC ANN. REP. 125 (1973) (319 applications for a total of \$14 million); 38 SEC ANN. REP. 124 (1972) (275 applications for a total of \$7 million); 37 SEC ANN. REP. 191 (1971) (223 applications for a total of \$7 million).

The SEC can also draw on its experience with allowances in its own reorganization proceedings under the Holding Company Act, 2 LOSS, *supra* note 5, at 762.

¹²⁸ The Commission itself is not eligible for compensation. Bankruptcy Act, § 242(2), 11 U.S.C. § 642(2) (1970).

¹²⁹ See, e.g., *In re Imperial "400" Nat'l Inc.*, 432 F.2d 232, 240 (3d Cir. 1970) ("Because of . . . [the SEC's] . . . experience in such matters, its impartiality, and its sole familiarity with the relevant facts in this case, its recommendations should be given great weight."); *In re TMT Trailer Ferry, Inc.*, 434 F.2d 804, 806-07 (5th Cir. 1970) (per curiam), *cert. denied*, 402 U.S. 907 (1971) ("The [SEC] having participated fully in these proceedings (now in their thirteenth year), from the very beginning of the filing of the chapter X reorganization, is intimately familiar with the services rendered by the Committee's counsel Therefore, the Court determined it "should follow the SEC recommendation . . . which we consider fair and reasonable"; *Scribner & Miller v. Conway*, 238 F.2d 905, 907 (2d Cir. 1956) (The court should follow the SEC's recommendations "unless the reorganization judge showed reasons otherwise based on specific findings."). But see *In re Yuba Consol. Indus., Inc.*, 260 F. Supp. 930, 950-51 (N.D. Cal. 1966) (criticism of SEC recommendations).

The Commission's recommendations, however, are advisory only and may not substitute for the independent judgment of the court. *Chicago & West Towns Rys. v. Friedman*, 230 F.2d 364, 368 (7th Cir. 1956), *cert. denied*, 351 U.S. 943 (1956). See S. REP. NO. 1916, 75th Cong., 1st Sess. 178 (1937); H.R. REP. NO. 1409, 75th Cong., 1st Sess. 45 (1937).

function of the dual purpose of the statutory fee provisions. On one hand, the Chapter X allowance machinery seeks to protect the assets of the reorganized corporation against unnecessary depletion.¹³⁰ On the other hand, it seeks to broaden the base of allowances to encourage more active participation by creditors, stockholders and their attorneys, thereby insuring that the reorganization proceedings are not dominated by a minority of the parties in interest.¹³¹ To effectuate these underlying purposes, the SEC, in rendering its recommendations to the court, has focused on three major issues: whether the services were compensable, whether the applicants are disinterested, and whether the amounts requested are reasonable.¹³² Furthermore, the Commission has participated most actively in cases requiring a construction of section 249¹³³ which disallows compensation to any applicant who has traded in the debtor's securities.¹³⁴ Nevertheless, categorization of the Commission's role is difficult. Aside from its uniformly rigorous review of allowance applications for evidence of possible conflict of interest¹³⁵ or inside

¹³⁰ Steinberg, *Salient Features in Awarding Allowances in Corporate Reorganization Proceedings and the Role of the Securities and Exchange Commission in Their Final Determination*, 8 N.Y. LAW FOR. 253, 266 (1962); Note, *The SEC and Allowances in Corporate Reorganization*, 42 GEO. L.J. 420, 424 (1954).

¹³¹ Steinberg, *Salient Features in Awarding Allowances in Corporate Reorganization Proceedings and the Role of the Securities and Exchange Commission in Their Final Determination*, 8 N.Y. LAW FOR. 253, 266 (1962). *Hearings on H.R. 6439*, 75th Cong., 1st Sess. 186 (1937) (statement of then SEC Commissioner, now retired Justice, Douglas). See 6A COLLIER ON BANKRUPTCY, ¶13.12 at 976-77 (14th ed. 1972) [hereinafter cited as COLLIER]. See also Teton, *Reorganization Revised*, 48 YALE L.J. 573, 603-04 (1939).

¹³² For a discussion of the factors to be considered in setting an award for compensation, see *In re Yuba Consol. Indus., Inc.*, 260 F. Supp. 930, 937-38 (N.D. Cal. 1966); Steinberg, *Salient Features in Awarding Allowances in Corporate Reorganization Proceedings and the Role of the Securities and Exchange Commission in their Final Determination*, 8 N.Y. L. FOR. 253, 270-75 (1962).

In addition to making recommendations concerning the merits of particular claims, the Commission also may comment on the feasibility of awarding the total requested claims in view of the particular status of the debtor's finances. Note, *The Role of the SEC in Corporate Reorganizations Under the Bankruptcy Act*, 1958 U. ILL. L. FOR. 631, 641 (1958).

¹³³ Section 249, 11 U.S.C. § 649 (1970) provides:

Any persons seeking compensation for services rendered or reimbursement for costs . . . incurred . . . shall file with the court a statement . . . [of] claims against, or stock of, the debtor . . . in which a beneficial interest . . . has been acquired or transferred . . . after the commencement of such proceedings. No compensation or reimbursement shall be allowed to any . . . person acting . . . in a fiduciary capacity, who [has traded in] such claims or stock . . . without the prior consent or subsequent approval of the judge . . .

¹³⁴ Note, *The SEC and Allowances in Corporate Reorganization*, 42 GEO. L. J. 420, 427 (1954).

¹³⁵ The Supreme Court has long been of the view that "'reasonable compensation for services rendered' necessarily implies loyal and disinterested service in the interest of those for whom the claimant purported to act." *Wood v. City Nat'l Bank & Trust Co.*, 312 U.S. 262, 268 (1941). For an example of a case where the SEC successfully challenged allowances to applicants with conflicts of interest, see *London v.*

trading,¹³⁶ its position varies as it attempts, in different fact situations, to effectuate the somewhat conflicting purposes of the fee provisions of the statute. Thus, in the name of the economy, the SEC has participated in numerous cases with the end of eliminating claims that are excessive¹³⁷ or that seek compensation for services that are suspect, not beneficial to the estate or only tenuously connected with the reorganization.¹³⁸ At the same time, with the end of encouraging increased participation, the SEC also has appeared to argue the necessity of higher fees¹³⁹ and to support the recognition of the rights of a larger class of claimants.¹⁴⁰ However, the courts' natural predilection for economy¹⁴¹ suggest that the Commission's influence may be more

Snyder, 163 F.2d 621, 626 (8th Cir. 1947). The SEC's advisory recommendations on awards for allowances from the debtor's estate are one of its most effective sanctions in monitoring the qualification and performance of fiduciaries.

¹³⁶ See Note, *The SEC and Allowances in Corporate Reorganization*, 42 GEO. L.J. 420, 433 (1954). The Supreme Court has decided that § 249 must be strictly construed. *Wolf v. Weinstein*, 372 U.S. 633, 654-56 (1963). See generally Troiano, *Bankruptcy Act—Section 249 of Chapter X—Disallowance of Compensation to Fiduciary for Trading in Stock of Debtor during Corporate Reorganization—"Uncompromised Rigidity"*, 34 BROOKLYN L. REV. 179 (1968).

¹³⁷ *In re TMT Trailer Ferry, Inc.*, 434 F.2d 804, 806-07 (5th Cir. 1970) (per curiam), cert. denied, 402 U.S. 907 (1971), *In re Imperial "400" Nat'l, Inc.*, 432 F.2d 232, 234 (3d Cir. 1970). *Yale Express Sys., Inc.*, (S.D.N.Y. No. 65-B-404), reported in 40 SEC ANN. REP. 130 (1974). *In re Yuba Consolidated Indus., Inc.*, 260 F. Supp. 930, 966 (N.D. Cal. 1966).

¹³⁸ *In re Postal Tele. & Cable Corp.*, 119 F.2d 861, 863 (2d Cir. 1941) (compensation denied attorney of debtor who worked with committee in opposing unsuccessfully, adoption of a plan); *Four Seasons Nursing Centers of Am., Inc.*, (W.D. Okla., No. BK 70-1008), reported in 39 SEC ANN. REP. 125-26 (1973) (recommending reduction in allowances claimed by indenture trustee who spent a large portion of its time reviewing papers filed by others in the proceeding and many of whose efforts duplicated the activities of its counsel). Similarly, the SEC will contest allowances made without adequate compliance with the mandatory notice provisions. *In re Cybern Educ., Inc.*, 478 F.2d 1340, 1344-45 (7th Cir. 1973) (per curiam).

¹³⁹ *In re Farrington Mfg. Co.*, (4th Cir., No. 75-1355), reported in 41 SEC ANN. REP. 157 (1975); *In re General Economics Corp.*, 360 F.2d 762, 764 (2d Cir. 1966). In *In re Farrington*, the Commission supported an appeal from an order of allowance for services taken by counsel to the trustee and urged that trustee's counsel was a court-appointed officer entitled to reasonable compensation, not a volunteer who is compensated on the basis of the benefit to the estate. 41 SEC ANN. REP. 157 (1975). In particular, the Commission cited three factors which it argued that the district judge had failed to balance against the needs for economy: (1) the importance of awarding reasonable compensation in cases where the standard of counsel's performance was not questioned in order to encourage the participation of competent counsel; (2) the crucial importance of the section 167 investigation and (3) that the result of the investigation and of the trustee's participation in certain lawsuits was to increase both participation in the plan and the distribution to creditors. *Id.*

¹⁴⁰ See, e.g., *In re Farrington Mfg. Co.*, (4th Cir., No. 75-1355), reported in 41 SEC ANN. REP. 157 (1975); *In re Mt. Forest Fur Farms of Am.*, 62 F. Supp. 59 (S.D. Mich. 1945), *aff'd*, 157 F.2d 640 (6th Cir. 1946).

¹⁴¹ See *Callaghan v. Reconstruction Fin. Corp.*, 297 U.S. 464, 468-69 (1936); Note, *The SEC and Allowances in Corporate Reorganization*, 42 GEO. L.J. 420, 424 (1954). Courts, for example, do not hesitate to award allowances lower than those recommended by the Commission. See, e.g., *In re Coast Investors, Inc.*, 388 F.2d 622, 626-27 (9th Cir. 1968).

strongly felt when exercised in the promotion of that purpose.¹⁴²

II. CHAPTER XI ARRANGEMENTS

There is a marked contrast between the procedures of Chapter X which contemplate "reorganization in the grand manner"¹⁴³ and the more summary provisions of Chapter XI.¹⁴⁴ In contrast to the broader scope of Chapter X which is carefully designed to protect the interests of stockholders and creditors,¹⁴⁵ Chapter XI simply affects the rights of "general creditors who have been deemed by Congress to need only the minimal disinterested protection provided by that chapter."¹⁴⁶ Accordingly, for all practical purposes, the entire Chapter XI proceeding is in the hands of the debtor who generally remains in possession,¹⁴⁷ operates the business¹⁴⁸ and proposes the arrangement.¹⁴⁹ Furthermore, little independent oversight is contemplated by Chapter XI, in that it makes no provision for a study of the debtor by a trustee, nor does it authorize the court to approve the plan or to communicate its advice to creditors in advance of the debtor's solicitation of their acceptances.¹⁵⁰ These summary pro-

¹⁴² Note, *The SEC and Allowances in Corporate Reorganization*, 42 GEO. L.J. 420, 427 (1954).

¹⁴³ Rostow & Cutler, *Competing Systems of Corporate Reorganization: Chapters X and XI of the Bankruptcy Act*, 48 YALE L.J. 1334 (1939).

¹⁴⁴ For a comparison of the different characteristics of Chapters X and XI, see *SEC v. American Trailer Rentals Co.*, 379 U.S. 594, 603-07 (1965); REPORT OF THE COMMISSION ON THE BANKRUPTCY LAWS OF THE UNITED STATES, H.R. DOC. NO. 93-137, 93d Cong., 1st Sess. part I, 244-45 (1973) [hereinafter cited as BANKRUPTCY COMMISSION REPORT].

¹⁴⁵ *SEC v. American Trailer Rentals Co.*, 379 U.S. 594, 605 (1965). Chapter X reorganizations may affect the interests of both secured and unsecured creditors. Bankruptcy Act § 216(1), 11 U.S.C. § 616(1) (1970).

¹⁴⁶ *SEC v. American Trailer Rentals Co.*, 379 U.S. 594, 606-07 (1965). Chapter XI arrangements provide only for the adjustment of unsecured debt. Bankruptcy Act, § 356, 11 U.S.C. § 756 (1970).

¹⁴⁷ Bankruptcy Act, § 342, 11 U.S.C. § 742 (1970); *SEC v. American Trailer Rentals Co.*, 379 U.S. 594, 606 (1965). The debtor remains in possession unless a trustee or receiver is appointed. Bankruptcy Act, § 342, 11 U.S.C. § 742 (1970). The court will appoint a trustee only in those very limited situations where a trustee in bankruptcy has previously been appointed. *Id.*, §§ 321, 332, 11 U.S.C. §§ 721, 732 (1970). The court "may" appoint a receiver upon application of any party in interest if it finds such appointment to be "necessary." *Id.*, § 332, 11 U.S.C. § 732 (1970).

¹⁴⁸ *Id.*, §§ 342, 343, 11 U.S.C. §§ 742, 743 (1970). Authorization to operate the business must be obtained from the bankruptcy court. Ch. XI R. 11-23.

¹⁴⁹ *Id.*, §§ 306(1), 323, 357, 11 U.S.C. §§ 706(1), 723, 757 (1970).

¹⁵⁰ The debtor may solicit acceptances of the plan of arrangement even before the filing of the proceeding and must solicit them before the court's approval of the plan. *SEC v. American Trailer Rentals Co.*, 379 U.S. 594, 606 (1965); Bankruptcy Act, § 336(4), 11 U.S.C. § 736(4) (1970); see note 175 *infra*. In addition, creditors have only the choice of accepting or rejecting the plan. *SEC v. American Trailer Rentals Co.*, 379 U.S. 594, 606 (1965).

Furthermore, while Chapter X applies the absolute priority rule, Chapter XI tests the fairness of a plan as to general creditors against what they would receive in a liquidation. BANKRUPTCY COMMISSION REPORT, *supra* note 144, at 245.

cedures, however, are consistent with the basic purpose of Chapter XI which is "to provide a quick and economical means of facilitating simple compositions among general creditors"¹⁵¹

The significant differences in both the scope and source of the Commission's involvement in Chapter X and Chapter XI cases reflect the distinct character of the two proceedings. While the SEC, by statutory mandate,¹⁵² plays a major role under Chapter X, the Commission's involvement is far more restricted in the simpler, more expedited procedures of Chapter XI. Its statutory role, in fact, simply reflects the fact that the choice between proceeding under Chapter X or Chapter XI is not optional with the debtor. Indeed, "Congress has made it quite clear that [they] are not alternate routes," but instead constitute "legally, mutually exclusive paths to attempted financial rehabilitation."¹⁵³ Thus, Chapter XI only expressly grants standing to the Commission for the purpose of making a conversion motion "to have the case proceed under Chapter X"¹⁵⁴ In *SEC v. American Trailer Rentals Co.*,¹⁵⁵ however, the Supreme Court expanded the Commission's Chapter XI role and held that "under the statutory scheme, while not charged with express statutory rights and responsibilities . . . , the SEC is entitled to intervene and be heard in a Chapter XI proceeding."¹⁵⁶ Although the Commission, in the past,

¹⁵¹ *SEC v. American Trailer Rentals Co.*, 379 U.S. 594, 606-07 (1965).

¹⁵² See text & notes 24-33 & 100-09 *supra*.

¹⁵³ *SEC v. American Trailer Rentals Co.*, 379 U.S. 594, 607 (1965). Proceedings under Chapter XI may be dismissed, or in effect transferred, if they "should have been brought" under Chapter X. Bankruptcy Act, § 328, 11 U.S.C. § 728 (1970). Similarly, a Chapter X petition will be deemed not to have been filed in good faith, and therefore will be subject to dismissal, if "adequate relief would be obtainable" under Chapter XI. *Id.*, §§ 141, 146(2), 11 U.S.C. §§ 541, 546(2) (1970).

¹⁵⁴ Bankruptcy Act, § 328, 11 U.S.C. § 728 (1970). Section 328 provides in part, that

[t]he judge may, upon application of the Securities and Exchange Commission or any party in interest, and upon such notice to the debtor, to the Securities and Exchange Commission, . . . if he finds that the proceedings should have been brought under Chapter 10 . . . , enter an order dismissing the proceedings under this Chapter

In 1940, the Supreme Court, in *SEC v. United States Realty & Improvement Co.*, held that the Commission could properly intervene in Chapter XI proceedings to advocate dismissal of the case on the ground that Chapter XI, when compared to Chapter X, was inadequate to protect public investors. 310 U.S. 434, 458 (1940). When Congress amended Chapter XI in 1952, it specifically codified this holding in § 328. Act of July 7, 1952, c. 579, § 30, 66 Stat. 432.

Under Ch. XI R. 11-15, which became effective as of July 1, 1974, the Commission or other party in interest, has 120 days from the first date set for the first meeting of creditors to file a motion, which time may be extended for good cause. The debtor, however, may move for transfer to Chapter X at any time. Because the Rule requires a showing that the case may properly proceed under Chapter X, in effect, the court can grant the motion only if it finds both that Chapter XI is inadequate and that Chapter X is feasible. 41 SEC ANN. REP. 158 (1975).

¹⁵⁵ 379 U.S. 594 (1965).

¹⁵⁶ *Id.* at 613.

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has played a more limited role in Chapter XI cases,¹⁵⁷ this difference in the scope of its involvement may tend to narrow in practice as the SEC's role in Chapter XI expands to reflect the fact that larger corporations, with more extensive public holdings, increasingly rely on Chapter XI as the vehicle for their rehabilitation.¹⁵⁸ Nevertheless, the two central issues with respect to the SEC's role in Chapter XI cases continue to be those surrounding its decisions of when to petition for conversion to Chapter X and whether to intervene in the Chapter XI proceeding.

A. Conversion Motions

Delineation of the factors that the Commission considers important in determining whether to move for conversion is essential because there is no clear standard for choosing between Chapters X and XI other than the vague "needs to be served" test¹⁵⁹ and because the Commission is often the sole participant advocating removal.¹⁶⁰ The courts have consistently rebuffed the SEC's position that the mere presence of numerous public investors is alone sufficient to mandate resort to Chapter X.¹⁶¹ Nevertheless, large

¹⁵⁷ See *Manufacturers' Credit Corp. v. SEC*, 395 F.2d 833, 842 (3d Cir. 1968), where the court noted that the SEC's standing to intervene in Chapter XI cases "should not be equated with the SEC's full power to investigate and report under Chapter X"

¹⁵⁸ BANKRUPTCY COMMISSION REPORT, *supra* note 144, at 246. Although proponents of Chapter XI generally laud its speed and economy, the real reason underlying the preference for Chapter XI is the extent of control retained by the debtor under that chapter. *Id.* at 247. For the suggestion that the Supreme Court, in granting the SEC standing to intervene in Chapter XI cases, did not contemplate a comparable degree of administrative participation, see text *infra* at note 196.

¹⁵⁹ See *American Trailer Rentals Co.*, 379 U.S. at 610; *General Stores, Inc. v. Schlensky*, 350 U.S. 462, 466 (1956).

The "needs to be served" test was first applied by Justice Douglas in *General Stores* where he noted that neither the character of the debtor, nor its capital structure was the controlling consideration. 350 U.S. at 466. Instead, he observed that

(i)t may well be that in most cases where the debtor's securities are publicly held c. X will afford the more appropriate remedy. But that is not necessarily so. A large company with publicly held securities may have as much need for a simple composition of unsecured debts as a smaller company. And there is no reason . . . why c. XI may not serve that end. The essential difference is not between the small company and the large company but between the needs to be served. *Id.*

The "needs" identified by Justice Douglas which might mandate the use of Chapter X include: the necessity of sacrifice by the stockholders and the need for an accounting by the management for misdeeds or for new management. *Id.*

¹⁶⁰ See Weintraub & Levin, *Chapter VII (Reorganizations) as Proposed by the Bankruptcy Commission: The Widening Gap Between Theory and Reality*, 47 AM. BANKR. L.J. 323, 324 (1973). Occasionally, when other parties petition for review on the ground that a proceeding under Chapter XI should have been brought under Chapter X, the SEC may appear in support of the court's jurisdiction to confirm the arrangement. See *In re Posi-Seal Int'l, Inc.*, 457 F.2d 237, 238-39 (2d Cir. 1972) (per curiam).

¹⁶¹ See, e.g., *American Trailer Rentals Co.*, 379 U.S. at 607, 611; *General Stores, Inc. v. Schlensky*, 350 U.S. 462, 466 (1956); *In re Lea Fabrics, Inc.*, 272 F.2d 769, 771 (3d

public holdings clearly invite close SEC scrutiny¹⁶² as the Commission continues to stress the number and sophistication of the debtor's public investors in advocating removal.¹⁶³ Furthermore, on a case by case basis, the Commission successfully has argued the significance of the fact that the debtor's rehabilitation requires "a substantial adjustment of widely-held public debt."¹⁶⁴ Additional criteria stressed by the SEC in arguing for removal include the need either for new competent management¹⁶⁵ or for a thorough investigation of the debtor by an independent trustee.¹⁶⁶ A successful petition for conversion will serve to address these problems because Chapter X may require the appointment of a disinterested trustee to take possession of the assets of the debtor,¹⁶⁷ whereas Chapter XI generally permits the debtor to continue in possession subject to the supervisory control of the court.¹⁶⁸ Furthermore, the Commission is likely to press for removal where the possibility of federal securities laws violations raises the question of whether these contingent claims

Cir. 1959), *appeal vacated as moot sub nom.* SEC v. Lea Fabrics, Inc., 363 U.S. 417 (1960); SEC v. Liberty Baking Corp., 240 F.2d 511, 514 (2d Cir.), *cert. denied*, 353 U.S. 930 (1957). When the Court in *General Stores*, *supra*, rejected the Commission's position that the presence of publicly held securities was determinative, the SEC introduced corrective legislation to preclude resort to Chapter XI by a corporate debtor that had securities owned by 100 or more persons. See 6 SEC ANN. REP. 55-57 (1940). The legislation did not pass. BANKRUPTCY COMMISSION REPORT, *supra* note 144, at 246.

¹⁶² 8 COLLIER, *supra* note 131, ¶ 4.22 at 467. See *American Trailer Rentals Co.*, 379 U.S. at 614.

¹⁶³ 40 SEC ANN. REP. 131-33 (1974). See *Norman Fin. & Thrift Corp. v. SEC*, 415 F.2d 1199, 1203 (10th Cir. 1969) (unsophisticated depositors in "Thrift Saving Accounts").

¹⁶⁴ *Manufacturers' Credit Corp. v. SEC*, 395 F.2d 833, 843 (3d Cir. 1968); *In re Arlan's Dept. Store*, 373 F. Supp. 520, 524-25 (S.D.N.Y. 1974). See *American Trailer Rentals Co.*, 379 U.S. at 614, 615; SEC v. Canandaigua Enterps. Corp., 339 F.2d 14, 19-20 (2d Cir. 1964).

¹⁶⁵ See, e.g., *American Trailer Rentals Co.*, 379 U.S. at 614-15; *Norman Fin. & Thrift Corp. v. SEC*, 415 F.2d 1199, 1204 (10th Cir. 1969); SEC v. Crumpton Builders, Inc., 337 F.2d 907, 911-12 (5th Cir. 1964); cf. *In re Meister Brau, Inc.*, 355 F. Supp. 515, 517 (N.D. Ill. 1972) (mem.) (petition filed by debtor's shareholders; SEC took no position on the merits of the petition. *Id.* at 517 n.3).

¹⁶⁶ See, e.g., *American Trailer Rentals Co.*, 379 U.S. at 615; *Norman Fin. & Thrift Co. v. SEC*, 415 F.2d 1199, 1204 (10th Cir. 1969); SEC v. Liberty Baking Corp., 240 F.2d 511, 515 (2d Cir.), *cert. denied*, 353 U.S. 930 (1957). One commentator has argued that evidence of past corporate mismanagement should be the determining factor in choosing between Chapters X and XI. See Katskee, *The Calculus of Corporate Reorganization Chapter X v. XI and the Role of the SEC Assessed*, 45 AM. BANKR. L.J. 171, 189-90 (1971).

In some cases, however, courts have refused to transfer a Chapter XI arrangement, and have discounted the necessity of a trustee's investigation on the grounds that an investigation accomplished by the referee would be sufficient. See *In re American Guaranty Corp.*, 221 F. Supp. 961, 967 (D. R.I. 1963). Cf. *In re Lea Fabrics*, 272 F.2d 769, 772 (3d Cir. 1959), *vacated as moot sub nom.* SEC v. Lea Fabrics, Inc., 363 U.S. 417 (1960) (*per curiam*).

¹⁶⁷ See text at notes 36-37 *supra*.

¹⁶⁸ See note 147 *supra*. For a comparison of these aspects of Chapters X and XI, see *American Trailer Rentals Co.*, 379 U.S. at 606.

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can be discharged under the limited scope of Chapter XI.¹⁶⁹ By moving for conversion to Chapter X, the SEC facilitates the adjudication of contingent securities fraud claims and their inclusion in the Chapter X plan of reorganization.¹⁷⁰

The SEC's ability to petition for conversion from Chapter XI to Chapter X is critical to its ability to protect the interests of public investors. Although there is no absolute rule that Chapter X must be used when the debtor is publicly owned, Chapter X, nevertheless, is generally the "appropriate proceeding for adjustment of publicly held debt."¹⁷¹ By seeking to insure that the rehabilitation of corporate debtors with widespread public holdings proceed under Chapter X, the SEC guarantees that the interests of public investors will be safeguarded by the more extensive provisions for disinterested protection included in that chapter.

B. Intervention by the SEC

In cases where the Commission has determined not to exercise its statutory authority to petition for a conversion to Chapter X, it nevertheless is crucial to identify those factors which may lead it to exercise its judicial grant of standing to intervene. In the past, the Commission has intervened most frequently in Chapter XI cases where the plan of arrangement contemplates the issuance of securities.¹⁷²

The likelihood that a proposal to issue securities pursuant to a plan of arrangement will trigger SEC intervention highlights one of the critical differences between Chapter X and Chapter XI. The issuance of securities pursuant to a Chapter X reorganization plan is hedged with statutory protective devices. Thus, there can be no solicitation of acceptances of the Chapter X reorganization plan until *after* it has been approved by the court.¹⁷³ Furthermore, a wide range of disclosure information, including the opinion of the judge and any reports filed by the SEC, must be submitted to the creditors and stockholders in conjunction with the solicitation of their acceptances of the

¹⁶⁹ See, e.g., *U.S. Fin., Inc.*, (S.D. Cal., No. 17007-K), reported in 41 SEC ANN. REP. 158-59 (1975); *Equitable Mortgage Inv. Corp.*, (S.D. Iowa, Nos. 74-509-C, 74-528-C, 74-537-C), reported in 41 SEC ANN. REP. 160-61 (1975). Under § 17a(2) of the Bankruptcy Act, 11 U.S.C. § 35(a)(2) (1970), fraud claims are not dischargeable in Chapter XI. As they are unliquidated and contingent, they also cannot be proved and therefore cannot be allowed. Bankruptcy Act, § 57(d), 11 U.S.C. § 93(d) (1970).

¹⁷⁰ A Chapter X proceeding is not limited to the adjustment of unsecured or fixed claims. On the contrary, it defines claims to "include all claims of whatever character . . . , whether or not such claims are provable . . . and whether secured or unsecured, liquidated or unliquidated, fixed or contingent." Bankruptcy Act, § 106(1), 11 U.S.C. § 506(1) (1970).

¹⁷¹ *American Trailer Rentals Co.*, 379 U.S. at 613.

¹⁷² The Commission staff has made a practice of communicating with referees around the country requesting notification of arrangements which may propose this type of issuance. 38 SEC ANN. REP. 130 n.60 (1972).

¹⁷³ Bankruptcy Act, § 176, 11 U.S.C. § 576 (1970).

plan.¹⁷⁴ In a Chapter XI case, however, there is a far greater potential for the issuance of deceptive securities. Acceptances of a Chapter XI plan of arrangement may be solicited even before the filing of the procedure and always before the court's approval of the plan.¹⁷⁵ Furthermore, the debtor who proposed the plan is also the one to solicit acceptances and such solicitation is accomplished with only limited judicial scrutiny.¹⁷⁶ This comparative lack of protection afforded public investors in the consummation of a Chapter XI plan of arrangement sensitizes the Commission to attempts to circumvent applicable provisions of the federal securities laws.¹⁷⁷

Because the Commission often intervenes expressly in order to thwart attempts to circumvent the federal securities laws, its role in Chapter XI cases is perhaps more narrowly directed to securing appropriate protection for the rights of the public investors in conjunction with the issuance of securities pursuant to a plan of arrangement. In particular, the SEC has characterized the purpose of its intervention in these circumstances as twofold. It seeks both

to develop the record as to adequacy of the disclosure of material facts and to assist the court in its task of scrutinizing securities which were to be issued pursuant to an arrangement and thus prevent the distribution of stock of doubtful value to an unsuspecting public.¹⁷⁸

As well as participating in order to insure adequate disclosure, the Commission also will intervene to challenge a plan on the grounds that it lacks the "good faith" required by section 366(4)¹⁷⁹ when the issuance of securities pursuant to the plan appeared to be motivated more by a desire to participate in a rising market than by a good faith attempt to resuscitate the debtor.¹⁸⁰

In addition to its efforts in monitoring the issuance of securities

¹⁷⁴ *Id.*, §§ 175, 176, 11 U.S.C. § 575, 576 (1970).

¹⁷⁵ *Manufacturers' Credit Corp. v. SEC*, 395 F.2d 833, 842 (3d Cir. 1968). Corotto, *SEC Reporting, Proxy and Antifraud Compliance—An Additional Perspective on Bankruptcy • Reorganization Proceedings*, 63 CALIF. L. REV. 1563, 1578-79 (1975) [hereinafter cited as Corotto].

¹⁷⁶ Corotto, *supra* note 175, at 1579. The application of SEC proxy requirements to Chapter X and XI plan solicitations reflects these differences in the statutory framework. Solicitations of acceptances of Chapter X plans are exempt from the proxy requirements under the Securities Exchange Act of 1934. Securities Exchange Act of 1934, R. 14a-2(e), 17 C.F.R. § 240.14a-2(e) (1974). Corotto, *supra* note 175, at 1580-81. However, these proxy requirements may apply to the debtor's solicitation of consents under Chapter XI. *Id.*

¹⁷⁷ The trustee, receiver or debtor in possession is responsible for compliance with the requirements of applicable state and federal laws. 6A COLLIER, *supra* note 131, ¶ 8.12 at 47-50. See Corotto, *supra* note 175, at 1567-71.

¹⁷⁸ *In re Puts & Calls, Inc.*, (C.D. Cal., No. 73-03706, 1973), reported in 40 SEC ANN. REP. 132 (1974).

¹⁷⁹ 11 U.S.C. § 766(4) (1970).

¹⁸⁰ *In re Alco Universal*, (W.D. Mich., No. 370-72-B5, 1972), reported in 39 SEC ANN. REP. 127 (1973).

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pursuant to the plan of arrangement, the Commission also assumes a familiar, albeit a more limited, role as expert advisor with respect to other issues arising in the course of a Chapter XI proceeding. Thus, in keeping with its practice in its appearances in Chapter X cases, the SEC is actively concerned with the status and performance of other parties in interest.¹⁸¹ The Commission, for example, often intervenes for the purpose of replacing a debtor continued in possession with a receiver,¹⁸² particularly in cases involving allegations of mismanagement,¹⁸³ or violations of federal securities laws.¹⁸⁴ Similarly, the SEC may assist the court in determining the qualifications of the attorney retained by the debtor.¹⁸⁵ Furthermore, the SEC may lend its investigative resources to the court. However, because Chapter XI makes no provision for an independent study by the court or a trustee or for the communication of their advice to creditors in advance of the acceptance of the plan,¹⁸⁶ the investigation conducted by the SEC in these circumstances is likely to be more limited¹⁸⁷ and to become significant primarily when the court is ruling on conversion petitions brought by another party.¹⁸⁸

¹⁸¹ The Commission's role, however, is perforce more limited because in Chapter XI there is no regulation of creditor representatives whereas Chapter X imposes fiduciary standards and full disclosure of relationships. *BANKRUPTCY COMMISSION REPORT*, *supra* note 144, at 245.

¹⁸² See, e.g., *In re Peoples Loan & Inv. Co.*, 410 F.2d 851, 854 (8th Cir. 1969) (The Court, however, adopted the recommendation of the referee and denied the SEC's motion.); *In re Investors' Equity, Inc.*, (S.D. Iowa, No. 74-464-C), reported in 41 SEC ANN. REP. 160-61 (1975).

¹⁸³ *In re American Beef Packers, Inc.*, (D. Neb., No. Bk-75-0-17) reported in 41 SEC ANN. REP. 160 (1975); *In re Investors' Equity, Inc.*, (S.D. Iowa, No. 74-464-C), reported in 41 SEC ANN. REP. 160-61 (1975).

¹⁸⁴ *In re Investors' Equity, Inc.*, (S.D. Iowa, No. 74-464-C), reported in 41 SEC ANN. REP. 160-61 (1975). Similarly, the fact that the debtor's management is the subject of investigation by other state and federal agencies is likely to be a significant factor. See *In re American Beef Packers, Inc.*, (D. Neb., No. Bk-75-0-17), reported in 41 SEC ANN. REP. 160 (1975).

¹⁸⁵ *In re Longchamps, Inc.*, (S.D.N.Y., No. 75-B-953), reported in 41 SEC ANN. REP. 162 (1975), the debtor sought to retain, as its counsel in the proceeding, a law firm which asserted a substantial secured claim for services rendered prior to the filing of the Chapter XI petition. When the court turned to it for advice, the SEC concurred with the court's decision disqualifying the firm on the grounds that questions might arise with respect to the amount of the firm's claim or the validity of its security interest. *Id.*

¹⁸⁶ *American Trailer Rentals Co.*, 379 U.S. at 606.

¹⁸⁷ *In re Meister Brau, Inc.*, (N.D. Ill., No. 72-B-3965), reported in 39 SEC ANN. REP. 127 (1973), for example, the SEC prepared an investigation at the request of the court which was prepared entirely from the debtor's records and other public information.

¹⁸⁸ See *In re Posi-Seal Int'l, Inc.*, 457 F.2d 237, 238-39 (2d Cir. 1972) (per curiam); *In re Meister Brau, Inc.*, (N.D. Ill., No. 72-B-3965), reported in 39 SEC ANN. REP. 127 (1973). In that case, in connection with a § 328 conversion motion filed by shareholders, the Commission conducted a preliminary investigation, but declined to take any position on the motion because of its doubts that the debtor could be reorganized. The court subsequently denied the motion and requested the SEC to continue its investigation. Ultimately, the debtor was adjudicated a bankrupt. *Id.*

The Commission also has intervened infrequently in conjunction with other matters arising in the course of the administration of the debtor's estate. It may appear to support¹⁸⁹ or to contest the jurisdiction of the bankruptcy court to take certain action. In *Cavanagh Communities Corp. v. New York Stock Exchange, Inc.*,¹⁹⁰ for example, the Commission filed an amicus curiae brief in support of the New York Stock Exchange's appeal from the bankruptcy court's order enjoining the Exchange from filing an application with the Commission to delist the debtor's common stock and convertible subordinated debentures.¹⁹¹ The bankruptcy judge had ruled that the stock exchange listing constituted "property" of the debtor which therefore fell within the exclusive jurisdiction of the court.¹⁹² On appeal, however, the court agreed with the SEC's contention that the bankruptcy court lacked jurisdiction because section 12(d) of the Securities Exchange Act of 1934¹⁹³ vests exclusive jurisdiction over the delisting process with the Commission.¹⁹⁴ In addition to concerning itself with jurisdictional matters, the SEC also has appeared to contest the sufficiency of consideration offered in a sale of major assets of the debtor.¹⁹⁵

Despite this evident variety of purposes for which the Commission will intervene in a Chapter XI case, its participation has been considerably more circumspect than the major role it has played in Chapter X reorganizations. This marked distinction in the scope of its involvement presumably results from three major factors. First, the vehicle for its participation is not an express statutory provision but is rather a judicial grant of standing to intervene. This judicial grant of standing is qualified by the Supreme Court's suggestion that it did not thereby indicate "the desirability of the [SEC's] performing its full Chapter X functions."¹⁹⁶ Second, Chapter XI itself offers less opportunity for intervention by a public agency because, consistent with its purpose of facilitating simple compositions among general creditors,¹⁹⁷ its procedures are more summary. Third, by pressing for conversion to Chapter X in cases which involve the substantial adjustment of widely held public debt,¹⁹⁸ the SEC itself may limit the necessity for subsequent appearance on behalf of public investors in

¹⁸⁹ *In re Posi-Seal Int'l, Inc.*, 457 F.2d 237, 238-39 (2d Cir. 1972) (per curiam).

¹⁹⁰ 422 F. Supp. 382 (S.D.N.Y. 1976). See 41 SEC ANN. REP. 161 (1975).

¹⁹¹ 422 F. Supp. at 384. See 41 SEC ANN. REP. 161 (1975).

¹⁹² *Id.* at 384.

¹⁹³ 15 U.S.C. § 781(d) (1970).

¹⁹⁴ 422 F. Supp. at 385-87.

¹⁹⁵ *In re Welfare Fin. Corp.*, (S.D. Ohio, No. 69085-6), reported in 40 SEC ANN. REP. 131 (1975).

¹⁹⁶ *American Trailer Rentals Co.*, 379 U.S. at 614 ("Where debt is publicly held, the SEC is likely, as here, to have become familiar with the debtor's finances, indicating the desirability of its performing its full Chapter X functions." (emphasis added)); *Manufacturers Credit Corp v. SEC*, 395 F.2d 833, 842 (3d Cir. 1968).

¹⁹⁷ See text *supra* at notes 146-51.

¹⁹⁸ See text *supra* at notes 159-71.

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Chapter XI proceedings. These three factors serve to indicate that while the restricted role assumed by the SEC in Chapter XI cases represents an accommodation with that chapter's more summary character, it does not necessarily entail any lapse in the agency's efforts to protect the public investor.

III. ROLE OF THE SEC UNDER PROPOSED REVISIONS OF THE BANKRUPTCY ACT

Recent proposed legislation aimed at revising the Bankruptcy Act raises the prospect of a substantial alteration of the Commission's current role in corporate reorganizations and arrangements. One bill, prepared by the Commission on the Bankruptcy Laws of the United States,¹⁹⁹ virtually abolishes the SEC's participation. It provides for the creation of a new administrative agency which would exercise the administrative functions now performed by bankruptcy judges and also would assume the Commission's present responsibilities. A second bill, proposed and introduced at the request of the National Conference of Bankruptcy Judges,²⁰⁰ makes more limited changes and apparently contemplates the SEC's continued participation in reorganization proceedings. The SEC is generally opposed to the alterations in its role as proposed in both pieces of legislation.²⁰¹ The most recent bill proposing revisions in the bankruptcy laws, introduced by Congressman Edwards in the 95th Congress,²⁰² appears to eliminate the SEC's advisory participation in administrative aspects of reorganization proceedings. At the same time, however, it would restructure the procedure governing the confirmation of the plan and explicitly provide for SEC participation at that time. The SEC has not yet commented officially on the substance of these proposed changes.

¹⁹⁹ The Commission on the Bankruptcy Laws of the United States was established by the Act of July 24, 1970, Pub. L. 91-354, 84 Stat. 468. The Commission Bill was originally introduced in the summer of 1973 as S. 2565, 93d Cong., 1st Sess. and H.R. 10792, 93d Cong., 1st Sess. (1973). It represents more than two years of intensive study, hearings and drafting. Levit, *Report of the Bankruptcy Committee of the Commercial Law League of America on Proposed Revisions of the Bankruptcy Act*, 80 COMM. L.J. 188 (1975). The Bankruptcy Commission's study and findings (Part I) and its proposed bill and notes (Part II) have been reprinted in the REPORT OF THE COMMISSION ON THE BANKRUPTCY LAWS OF THE UNITED STATES, Parts I and II, H.R. DOC. NO. 137, 93d Cong., 1st Sess. (1973) [hereinafter cited as BANKRUPTCY COMMISSION REPORT]. The bill was reintroduced as S. 236, 94th Cong., 1st Sess. (1975) by Senator Burdick and referred to the Committee on the Judiciary, 121 CONG. REC. 5429 (January 17, 1975). It was not reported out of committee and has not yet been reintroduced in the 95th Congress.

²⁰⁰ S. 4060, 93d Cong., 2d Sess. (1974); H.R. 16643, 93d Cong., 2d Sess. (1974). The bill was reintroduced as S. 235, 94th Cong., 1st Sess. (1975).

²⁰¹ See text and notes *infra* at 219-20 and 238-39.

²⁰² The bill was introduced by Congressman Edwards, of California, for himself and for Mr. Butler, as H.R. 6, 95th Cong., 1st Sess. (1977) [hereinafter cited as the Edwards Bill].

A. *The Bankruptcy Commission Bill*

The Bankruptcy Commission Bill, as first introduced in 1973, incorporates major substantive changes in the law of corporate reorganization, many of which stem from its proposed creation of a new administrative agency. The Commission recommends the severance of the administrative from the judicial functions within the bankruptcy system.²⁰³ Accordingly, its bill would create a new United States Bankruptcy Administration,²⁰⁴ to be operated through regional and local officers within the executive branch of the federal government. The Bankruptcy Administration would be "empowered to handle almost all matters in proceedings under the Act which do not involve litigation."²⁰⁵ The judicial functions, on the other hand, would be performed by bankruptcy judges appointed to bankruptcy courts also established by the Act.²⁰⁶

That the new Bankruptcy Administration effectively would supplant the SEC's present role in corporate reorganizations is most evident in the sections of the proposed Act governing the formulation of the plan. Although the bill would require a report regarding a plan to be submitted for a vote in every case where the plan would adversely affect any publicly held securities,²⁰⁷ it would transfer this function from the SEC to the new Bankruptcy Administration.²⁰⁸ The pro-

²⁰³ BANKRUPTCY COMMISSION REPORT, *supra* note 199, Part I, at 5-8.

The Commission concluded, in effect, that there was no reason to involve the judge in matters which were purely administrative in nature. *Id.* at 5. Furthermore, it found that there were substantial reasons for not entrusting litigation to bankruptcy judges who had previously been involved in the administration of the litigated estates. The tribunal's prior involvement in the resolution of administrative matters impaired the litigants' confidence in the impartiality of its decision of a subsequently litigated controversy. Also, it cast doubt on the court's ability to adjudicate that controversy solely from evidence presented to the trier. *Id.* Therefore, analogizing to the division of function between the Internal Revenue Service and the Tax Court, the Commission recommended the creation of a new agency to handle administrative matters and thereby implement the proposed severance of administrative and judicial functions. *Id.* at 6.

²⁰⁴ Commission Bill, §§ 3-101-3-403. BANKRUPTCY COMMISSION REPORT, *supra* note 199, Part III, at 51-66.

²⁰⁵ BANKRUPTCY COMMISSION REPORT, *supra* note 199, Part I, at 7.

²⁰⁶ Commission Bill, §§ 2-101-2-210; BANKRUPTCY COMMISSION REPORT, *supra* note 199, Part III, at 15-50.

²⁰⁷ Commission Bill, §§ 7-306, 7-307. The proposed act would define "publicly held securities" as meaning "securities of a class the ownership of which is held of record by 300 or more persons." *Id.*, § 1-102(36). This should be distinguished from the present practice which only requires the judge to submit the plan to the SEC for report if the scheduled indebtedness exceeds \$3,000,000. Bankruptcy Act, § 172, 11 U.S.C. § 572 (1976).

²⁰⁸ Commission Bill, § 7-306(b), provides that "[p]rior to the date set for the hearing on approval, the administrator shall file with the court an advisory report and a summary thereof concerning the plan and modifications" One commentator, noting a serious inconsistency in the statutory scheme, has questioned "by what sort of jurisdictional legerdemain" the court may approve or confirm a plan in a case pending before the Administrator. Lee, *A Critical Comparison of the Commission Bill and the Judges' Bill for the Amendment of the Bankruptcy Act*, 49 AM. BANKR. L.J. 1, 46 (1975) [hereinafter cited as Lee].

posed Act is somewhat less explicit as to the SEC's continued performance of those advisory functions which it presently assumes pursuant to its statutory authority to intervene.²⁰⁹ The bill clearly contemplates some continued participation by the SEC. It would provide that the SEC will continue to receive "written notice . . . of the commencement of a [reorganization] case . . . if the debtor is a corporation having 300 or more security holders and such other notices as it may request in connection with the case or a class of cases."²¹⁰ Furthermore, it would authorize the SEC, together with other agencies and persons given standing to intervene, to "appear and be heard in the bankruptcy court respecting any matter that arises in the administration of a case under Chapter VII," and enumerates a wide range of matters as to which the bill expressly contemplates their appearance.²¹¹ The Bankruptcy Commission, however, has described the purpose of these notice and standing provisions insofar as they apply to the SEC as being merely

to solicit the cooperation and aid of the Securities and Exchange Commission in any case where it has previously conducted an investigation of the affairs of the debtor corporation or where it may be peculiarly equipped to conduct such an investigation during the course of the proceedings.²¹²

Thus, it appears that the Commission's reading of the proposed Act would virtually eliminate SEC participation in corporate reorganizations except insofar as the SEC might appear in order to fulfill its responsibilities under the federal securities laws or might afford the Bankruptcy Administration the benefits of its prior discharge of its duties under those Acts.

In recommending that the new Bankruptcy Administration supplant the SEC, the Bankruptcy Commission, in effect, is attempting to

²⁰⁹ The Commission, however, explicitly contemplated that the Bankruptcy Administrator, rather than the SEC, would make recommendations concerning fee and expense applications. BANKRUPTCY COMMISSION REPORT, *supra* note 199, Part I, at 249.

²¹⁰ Commission Bill, § 7-107(c).

²¹¹ *Id.*, § 2-205(b).

The bill expressly accords standing to: the debtor, an indenture trustee, a creditor, an equity security holder, authorized committees, the administrator, the SEC and any State or Federal Commission having regulatory jurisdiction over a debtor that is a public utility. *Id.* The enumerated matters of administration include the appointment of an additional committee, the appointment or removal of a trustee, the dismissal or conversion of the case to one for liquidation, a sale of all or substantially all of the property of the estate, the approval and confirmation of the plan, and the setting aside of such order of confirmation.

²¹² BANKRUPTCY COMMISSION REPORT, *supra* note 199, Part I, at 26. See § 7-107(c), Advisory Committee note 4, which characterized the notice provision as enabling the SEC "to participate in any investigation where violations of federal securities law may have occurred and to make available to the trustee the information accumulated from any prior investigation by the Commission." See also § 7-306(b), Advisory Committee note 3, which notes that the "present Chapter X functions of the [SEC] are to be performed by the administrator."

give more comprehensive statutory recognition to the theory that corporate reorganizations are only incidentally law suits and, in fact, primarily constitute an exercise in corporate finance and management. In setting forth its rationale for supplanting the SEC, the Bankruptcy Commission began from the premise that the "requirement for the representation by a public agency of the public interest and the interest of public investors in a reorganization proceeding is essential."²¹³ For two reasons, however, it concluded that the Bankruptcy Administration should assume this responsibility.²¹⁴ First, the Commission reasoned that the SEC alone was not equipped to handle the wider grant of administrative responsibility envisioned by the Act. Although the SEC had played a "very constructive" role in Chapter X cases, that role had been "very limited,"²¹⁵ both because the SEC's participation in reorganization proceedings is "tangential to its major statutory duties" and because "that function has not been adequately funded in the past."²¹⁶ Therefore, the Commission concluded that these new responsibilities—the "general policies of all bankruptcy proceedings"—should be transferred to a new agency which "will be intimately involved and familiar with all aspects of all bankruptcy proceedings."²¹⁷ Secondly, the Commission determined that not only was the SEC ill-equipped to perform these *new* administrative functions but also that it should not continue to fulfill its former duties because "it would be undesirable for two agencies to perform similar functions."²¹⁸

Both reasons advanced by the Bankruptcy Commission in support of its recommendation to displace the SEC's role in corporate reorganizations are open to serious challenge. It is difficult to conceive of the SEC's role in Chapter X cases as "tangential" to its main duties because Chapter X, at least in part, is an investor protection statute.²¹⁹ Furthermore, if the SEC can be faulted for playing only a "limited" role, the appropriate solution would be to advocate increased funding.²²⁰ Further, it is not necessarily undesirable for two

²¹³ BANKRUPTCY COMMISSION REPORT, *supra* note 199, Part I, at 25-26.

²¹⁴ *Id.* at 26.

²¹⁵ *Id.* at 249.

²¹⁶ *Id.* at 26.

²¹⁷ *Id.* at 26, 249. In addition, the Commission noted that the new agency would be better able to obtain adequate funding for this particular function and to respond promptly when called upon to render an advisory report. *Id.* at 26. Furthermore, the proposed statute would authorize it to adopt rules and regulations governing the solicitation of acceptances of all reorganization plans. *Id.*

²¹⁸ *Id.* at 249.

²¹⁹ See *American Trailer Rentals Co.*, 379 U.S. at 614 ("Chapter X is one of the many Acts in which the SEC has the statutory right and responsibility to protect public investors," (footnote omitted)); REPORT OF THE SECURITIES AND EXCHANGE COMMISSION ON PROPOSED BANKRUPTCY LEGISLATION (S. 235 & S. 236), submitted to Subcommittee on Improvements in Judicial Machinery, Senate Committee on the Judiciary, December 8, 1975, at 16 [hereinafter cited as SEC REPORT ON PROPOSED LEGISLATION].

²²⁰ This is the position taken by the SEC. See SEC REPORT ON PROPOSED LEGISLATION, *supra* note 219, at 17.

agencies to perform similar functions as long as the focus of their role is different.²²¹ Rather than lose the substantial experience in corporate reorganizations acquired by the SEC, it seems preferable to allow it to continue to concern itself with the investor protection aspects of corporate reorganization proceedings.²²²

B. *The Judges' Bill*

The Bankruptcy Commission's proposal to establish a U.S. Bankruptcy Administration drew particularly angry criticism from the bankruptcy judges who had not been included in the Commission's membership.²²³ The National Conference of Bankruptcy Judges thereafter issued its own proposal (the Judges' Bill)²²⁴ which paralleled the Commission Bill in many respects,²²⁵ but recommended maintaining the judicial delivery system while shifting some administrative responsibilities from the bankruptcy judges to an administrative branch within the judiciary.²²⁶ The Judges' Bill would create within the Administrative Office of the United States Courts a Branch

²²¹ The Energy Supply and Environmental Coordination Act of 1974, 15 U.S.C. §§ 791-98 (Supp. V 1975) (ESECA), while totally unrelated to corporate reorganizations, provides an interesting example of a statutory framework which institutionalizes the participation of several administrative agencies in order to capitalize on their separate areas of expertise. The Act is designed to promote national energy self-sufficiency "in a manner which is consistent, to the fullest extent practicable, with existing national commitments to protect and improve the environment . . ." ESECA, § 1, 15 U.S.C. § 791 (Supp. V 1975). The statute, accordingly, is administered by the Federal Energy Administration (FEA) which is authorized to order any public utility to convert its primary energy source from gas or petroleum products to coal. *Id.*, § 2(a), 15 U.S.C. § 792(a) (Supp. V 1975). A prerequisite to the effectiveness of such a conversion order, however, is receipt by the FEA of notification from the Administrator of the Environmental Protection Agency (EPA) regarding the power plant's compliance with the applicable air pollution requirements. *Id.*, § 2(b)(3)(B), 15 U.S.C. § 792(b)(3)(B) (Supp. V 1975). Thus, the statute gives primary responsibility for the administration of the Act to one agency, but mandates the participation of another in order to ensure that the particular concerns of the latter agency are factored into the former's decisionmaking process.

²²² See SEC REPORT ON PROPOSED LEGISLATION, *supra* note 219, at 18, where the SEC comments "[i]f the Administrator is concerned with administrative matters for the bankruptcy system as a whole, there is no conflict if the SEC should continue to concern itself with the investor protection aspects of a reorganization proceeding."

²²³ 31 CONG. Q. ALMANAC 456 (94th Cong., 1st Sess., 1975).

²²⁴ The Judges' Bill was first introduced in the 93rd Cong., 2d Sess., as H.R. 16643 and S. 4060. Subsequently, it was reintroduced in the 94th Cong., 1st Sess., as S. 235.

²²⁵ For a comparison of the major differences between the two bills, see generally Lee, *supra* note 208. One critical distinction is that the Commission Bill would consolidate the present chapters X, XI and XII into a simple reorganization Chapter VII, whereas the Judges' Bill would combine Chapters XI and XII into a single chapter on arrangements but otherwise would maintain the current distinction between reorganizations and arrangements. *Id.* at 38.

²²⁶ 31 CONG. Q. ALMANAC 456 (94th Cong., 1st Sess., 1975). Both bills provide for the establishment of independent United States bankruptcy courts. Lee, *supra* note 208, at 1.

of Bankruptcy Administration.²²⁷ Through this Branch, the Director of the Administrative Office would enjoy primary responsibility for administrative matters such as the adoption of rules, the appointment of trustees and creditors' committees, and the receipt and disbursement of the funds of the debtor's estate.²²⁸ Thus, whereas the Commission Bill proposes a delivery system controlled by an Administrator exercising both administrative and judicial functions, the Judges' Bill would continue the present "court-oriented" delivery system under which the courts would merely delegate certain administrative responsibilities.²²⁹

Because the Judges' Bill retains the "court-oriented" delivery system, the Director of the Administrative Office would not usurp the SEC's current role. Instead, the Judges' Bill envisions the SEC's continued participation²³⁰ but effectuates certain important changes in the provisions governing the advisory report and the service of documents. With respect to the service of documents, the Judges' Bill eliminates the current requirement of section 265²³¹ which provides for the service of copies of all pleadings and orders on the SEC. Instead, the proposed bill merely requires that the SEC receive notices.²³² The Commission has criticized the change as likely to inhibit its efforts to identify cases appropriate for its intervention.²³³ In addition to changing the provision relating to service of documents, the Judges' Bill institutes two changes relating to the SEC's role in the confirmation of a plan of reorganization. Although it continues to provide that the SEC may file advisory reports on plans with the Court,²³⁴ the bill eliminates the present requirement²³⁵ that the Court *must* submit the proposed plan to the Commission for an advisory report if the corporation's scheduled indebtedness exceeds \$3,000,000.²³⁶ Secondly, the Judges' Bill indicates that the SEC's advisory report must be filed *before*, rather than after, the plan

²²⁷ Judges' Bill, Title II, §§ 206, 207. Lee, *supra* note 208, at 11-13.

²²⁸ Judges' Bill, Title II, §§ 206, 207. Lee, *supra* note 208 at 11-13.

²²⁹ Lee, *supra* note 208, at 13.

²³⁰ The bill provides for the SEC's right to be heard on any matter arising in the proceeding but omits the present language deeming the Commission to be "a party in interest." Judges' Bill, § 2-205. In addition, the bill continues to provide that the SEC or any party in interest may petition for the conversion of a case from the new Chapter VIII on arrangements to a reorganization proceeding under the new Chapter VII. Judges' Bill, § 8-201.

²³¹ Bankruptcy Act, § 265, 11 U.S.C. § 665 (1970).

²³² Judges' Bill, § 4-701(c).

²³³ SEC REPORT ON PROPOSED LEGISLATION, *supra* note 219, at 16. In addition, receipt of copies of the pleadings and orders enables the SEC to fulfill an important service for creditors and investors who can turn more conveniently to the Commission's public reference rooms than to the files of the clerk of the court where the case is pending. *Id.* Accordingly, the SEC recommends that the Judges' Bill, if enacted, should be amended to provide that it should receive all documents filed in the case. *Id.* at 19.

²³⁴ Judges' Bill, § 7-305.

²³⁵ Bankruptcy Act, § 172, 11 U.S.C. § 572 (1970).

²³⁶ Judges' Bill, § 7-305.

hearing.²³⁷ The SEC is strongly opposed to both these proposed changes.²³⁸ In particular, it contends that the time change for the filing of its advisory report is "critical" because a prehearing report would not provide much assistance to public investors since it would necessarily be limited to a textual analysis of a plan which is often revised in the course of the hearing and would fail to take into account the crucial evidence adduced at the hearing.²³⁹

Whether the Judges' Bill might effectuate other changes in the role of the SEC is somewhat unclear. The proposed legislation clearly envisions the SEC's continued participation insofar as it provides for the SEC's right to be heard on any matter arising in the proceeding.²⁴⁰ However, this provision authorizing the SEC to appear omits the language in the current Act²⁴¹ which deems the Commission a "party in interest."²⁴² Because many of its provisions are drawn in terms of a "party in interest,"²⁴³ this omission may suggest that the Judges' Bill intends to limit the SEC to presenting its views in the course of a motion made by another party rather than to petition on its own in the first instance for similar relief. Thus, whereas in proceedings under the present Chapter X the SEC can file a formal objection to the appointment of a trustee,²⁴⁴ the provisions of the Judges' Bill may indicate that it cannot *initiate* such action but instead is limited to presenting its views when the objection is raised by another party. If, indeed, this is the result intended, the change is probably motivated by the same sentiment which prompted the current Act's denial to the SEC of the right to appeal: a government agency should not be allowed to delay the proceedings when none of the parties with an economic interest in the proceeding have chosen to do so.²⁴⁵ Just as the denial of the right to appeal has been criticized as limiting the Commission's effectiveness,²⁴⁶ the failure to accord it status as a party in interest is equally likely to curtail its ability to protect public investors.

C. The Edwards Bill

The most recent proposed legislation seeking to revise the bank-

²³⁷ *Id.*, § 7-305(b).

²³⁸ SEC REPORT ON PROPOSED LEGISLATION, *supra* note 219, at 19. The Commission recommends retaining the provision for mandatory reference of plans to it for report where the liabilities exceed \$3,000,000. *Id.* It noted that it does not comment on all plans so referred and should be allowed to continue to exercise its discretion. *Id.*

²³⁹ *Id.*

²⁴⁰ See note 230 *supra*.

²⁴¹ Bankruptcy Act, § 208, 11 U.S.C. § 608 (1970).

²⁴² Judges' Bill, § 2-205.

²⁴³ *E.g.*, § 7-101(c) (provision for change in membership of official creditors' committee on application of party in interest when the committee is not representative of members of the class); § 7-102 (appointment of trustee without regard to amount of indebtedness).

²⁴⁴ See text *supra* at note 53.

²⁴⁵ See note 30 *supra*.

ruptcy laws is that introduced by Congressman Edwards in the 95th Congress.²⁴⁷ Like the Commission Bill and the Judges' Bill, the Edwards Bill provides for the creation of United States bankruptcy courts.²⁴⁸ Furthermore, the Edwards Bill, like the Judges' Bill, envisions the continuation of the present "court-oriented" delivery system. The administrative component of the Edwards Bill, however, is even more limited in authority than the Branch of Bankruptcy Administration within the Administrative Office of the United States Courts proposed by the Judges' Bill. The Edwards Bill creates an office of a United States trustee, appointed in each district by the United States Attorney General,²⁴⁹ who would operate under the general supervision of a Bankruptcy Division to be created in the Department of Justice.²⁵⁰ The duties of this United States trustee, in general, would be to "serve as and perform the duties of a trustee in a case under title 11 when required under title 11 to serve as trustee"²⁵¹ Although the bill confers certain additional specific authority upon the United States trustee,²⁵² the trustee would not exercise a general independent administrative authority which, for example, would authorize him to adopt bankruptcy rules.²⁵³ Furthermore, he would not serve as trustee in all cases arising under title 11 because the bill expressly declines to denominate him as the exclusive person eligible for such service.²⁵⁴ Thus, the Edwards Bill, in creating the United States trustee, does not thereby provide for the disinterested intervention of

²⁴⁶ *Id.*

²⁴⁷ Edwards Bill, *supra* note 202. The Edwards Bill is divided into four titles. Title I amends the Bankruptcy Act and would be codified in 11 U.S.C. Title II amends 28 U.S.C. and the federal rules of evidence. Title III amends the Internal Revenue Code. Title IV includes amendments to other acts.

²⁴⁸ *Id.* Title I, § 151.

²⁴⁹ *Id.*, Title III, § 581.

²⁵⁰ *Id.*, Title II, § 586(b).

²⁵¹ *Id.*, Title II, § 586(a)(1).

²⁵² The United States trustee, for example, may request that the court order the appointment of a trustee or an independent investigator. *Id.*, Title I, § 1104. Similarly, he may request that the court terminate the trustee's appointment and restore the debtor to possession. *Id.*, Title I, § 1105.

²⁵³ Compare provisions of the Judges' Bill governing the administrative authority of the Branch of Bankruptcy Administration at note 228 *supra*.

²⁵⁴ Section 321 would allow a person to serve as trustee when he is—"(1) an individual that is competent to perform the duties of trustee, and resides or has an office in the judicial district within which the case . . . is pending; (2) a corporation authorized by [its] charter or bylaws to act as trustee . . . ; or (3) the United States trustee for such judicial district."

Significantly, there is no floor on the amount of a corporation's indebtedness below which consideration of the appointment of a trustee is unwarranted. *Id.*, Title I, § 1104. Instead, a court "may order the appointment of a trustee if—(1) the protection afforded by a trustee is needed; and (2) the costs and expenses of a trustee would not be disproportionately higher than the value of the protection afforded." *Id.* Compare, for example, § 7-102(a) of the Commission Bill which authorizes the administrator to apply to the court to determine whether a trustee should be appointed when "the debtor is a corporation having debts of \$1,000,000 or more and three hundred or more security holders."

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a public agency on the same scale as would the Commission Bill and the Judges' Bill in establishing, respectively, the Bankruptcy Administration and Branch of Bankruptcy Administration within the Administrative Office of the United States Courts.

The Edwards Bill, on the other hand, does contemplate an extensive role for the SEC, at least in connection with the procedures leading to the confirmation of the plan of reorganization. The bill expressly provides for SEC participation at two crucial stages in the process: the solicitation of acceptances to the plan and the hearing on its confirmation. Thus, the SEC first may become involved in order to monitor the adequacy of the disclosures made to creditors who are being solicited to accept or reject the plan. Section 1125(b) provides that "[a]n acceptance or rejection of a plan may not be solicited . . . from a holder of a claim or interest . . . unless . . . there is transmitted to such holder the plan or a summary of the plan, and a written disclosure statement approved, after notice and a hearing, by the court as containing adequate financial information about the debtor."²⁵⁵ While the court, therefore, need not approve the plan itself before the solicitation of acceptances, it must approve the written disclosure statement and can only do so once it has held a hearing and determined that the statement meets the statutory disclosure standard.²⁵⁶ Furthermore, the bill provides that the SEC may appear and be heard at the hearing on the adequacy of the written disclosure statement.²⁵⁷

²⁵⁵ *Id.*, Title I, § 1125(b).

²⁵⁶ The bill defines "adequate financial information about the debtor" to mean: information of a kind, and in sufficient detail, as far as is reasonably practicable in light of the nature and history of the debtor and the condition of the debtor's books and records, as would enable a hypothetical reasonable investor typical of holders of claims or interests of the relevant class to make an informed judgment about the plan . . . " *Id.*, § 1125(a)(1).

²⁵⁷ Section 1125(d) provides that [s]olicitation . . . is not governed by any otherwise applicable nonbankruptcy law, rule or regulation, but an agency or official whose duty is to administer or enforce such law, rule or regulation may be heard on the issue of whether a disclosure statement contains adequate financial information about the debtor. Such an agency or official may not appeal from an order approving a disclosure statement.

Since the proposed provision is conditioned on a finding that the SEC, or other agency, is subject to the duty of administering or enforcing a law or regulation which otherwise would be applicable to the solicitation, there might be situations in which the SEC could not participate because the federal securities laws and rules and regulations issued thereunder would *not* otherwise be applicable to the proxy solicitation of acceptances or rejections of the plan of reorganization. For example, under the current Act, the proxy requirements of the Securities Exchange Act of 1934 do not apply to solicitations of a Chapter X plan because a limited exemption has been provided in recognition of the fact that the Chapter X provision for transmitting the SEC's own report and recommendations largely negate the necessity of complying with the statutory proxy requirements. Securities Exchange Act of 1934, R. 14a-2(e), 17 C.F.R. § 240.14a-2(e) (1974). These same proxy requirements do apply, however, to the solicitation of consents in a Chapter XI case. See Corotto, *supra* note 72, at 1581. As the present exemption which applies to solicitations of a Chapter X plan is conditioned on the adequacy of the disclosure already provided by the Bankruptcy Act, it would seem that the Edwards'

In addition to authorizing the SEC to appear in order to ensure the adequacy of the disclosure statement, the Edwards Bill also entitles it to appear at the hearing on the plan and to object to its confirmation.²⁵⁸ Because the bill enumerates a wide range of requirements which the plan must meet to entitle it to judicial confirmation, the provision allowing the SEC to object to its confirmation effectively gives it leeway to express its view on a considerable number of issues arising in the course of the reorganization proceedings.²⁵⁹

While the Edwards Bill permits a two-step appearance by the SEC in conjunction with the plan of reorganization and thereby guarantees more effective protection of the interests of public investors, it does not expressly permit the SEC to continue to appear and be heard in connection with the variety of issues arising in the course of the administration of the debtor's estate. Unlike the Judges' Bill and the Commission Bill, the Edwards Bill does not contain any general grant of standing to the SEC.²⁶⁰ The bill's failure to provide for standing unnecessarily would hinder the SEC in its ability to safeguard the interests of public investors. The role of the United States trustee envisioned by the bill is not necessarily so extensive as to render the SEC's performance of its advisory role merely duplicative. Nor can the provisions for its appearance, however extensive, in connection with the acceptance and confirmation of the plan obviate the necessity for impartial representation during the earlier administration of the debtor's estate. On the contrary, the SEC, for example, views its current role with respect to those administrative matters as serving to prevent the confirmation of the plan from becoming little more than a ratification of a *fait accompli*.²⁶¹ If the bill proponents, however, are concerned that SEC intervention in these earlier stages of a corporate reorganization operates to add unnecessary expense and delay to the proceedings, a possible compromise is suggested by the Judges' Bill which apparently would allow the SEC to present its views only in the course of an objection raised by another party in in-

Bill would not intend both to declare that the proxy requirements of the federal securities laws did not govern the solicitation of acceptances and also to use that same declaration of inapplicability as a basis for denying the SEC's right to appear in order to ensure compliance with the standards imposed by the bill itself. A full discussion of the exemption from federal securities laws established in these proposed bills is beyond the scope of this article. For an analysis of the exemption provisions of the Judges' Bill and the Commission Bill, see SEC REPORT ON PROPOSED LEGISLATION, *supra* note 219, at 101-112.

²⁵⁸ Edwards Bill, *supra* note 202, Title I, § 1128(b).

²⁵⁹ *Id.*, § 1129. The requirements include, for example, the necessity of finding that payment of allowances made before the confirmation of the plan were reasonable. *Id.*, § 1129(a)(4).

²⁶⁰ A conversation the author had with congressional staff counsel on March 22, 1976 suggests that the Edwards Bill, in fact, may be revised to grant the Commission standing.

²⁶¹ See, in particular, its position on the sale of all or a substantial part of the debtor's assets when the sale is not made pursuant to a plan of reorganization, as discussed in the text *supra* at notes 90-99.

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terest and not to petition on its own in the first instance for similar relief. Although this restriction may limit the SEC's effectiveness, to some extent it would continue to afford the participants, and the court, the benefit of the expertise acquired by the SEC in nearly forty years of such appearances.

CONCLUSION

Because corporate reorganizations and arrangements present what is fundamentally an administrative problem in corporate finance and management, the SEC has assumed a major role under Chapter X and Chapter XI of the Bankruptcy Act. The Commission's function resembles that of an *amicus curiae* which monitors the performance and qualification of other parties in interest, acts as an impartial representative of public investors and provides expert assistance to the court. The general consensus is that:

the service being rendered by the Commission to the Courts in connection with the reorganization of corporations [is] most valuable, if not indispensable, for the proper disposition of this vital segment of court business according to the Congressional intent. The Commission affords the necessary expert knowledge, the skill, and the uniform approach which individual justices cannot have; . . . the assistance is unique in its usefulness, and not otherwise to be obtained. The judge is not bound to observe all suggestions of the Commission, but the very fact that he has them before him is assurance of his complete preparation for adjudication, with the public interest adequately protected.²⁶²

In light of the extent to which the SEC's participation has been welcomed by the federal judiciary, the alterations in its role envisioned by proposed legislation aimed at revising the Bankruptcy Act warrant careful scrutiny. Rather than lose the benefit of the substantial expertise acquired by the SEC, such legislation should seek to secure the SEC's continued participation in corporate reorganization proceedings. Therefore, in order to ensure the SEC's ability to continue to concern itself with the investor protection aspects of these proceedings, the proposed amendments should accord the SEC standing to intervene and also should institutionalize its participation in conjunction with the confirmation of the plan.

²⁶² 21 SEC ANN. REP. 89 (1955), *quoting* a comment received from Chief Judge Charles E. Clark, written on behalf of all the judges of the Second Circuit Court of Appeals. The Commission had sought comments from the federal judiciary in connection with a reappraisal of its functions in corporate reorganization proceedings.