Chapter 11F: A Proposal for the Use of Bankruptcy to Resolve (Restructure, Sell, or Liquidate) Financial Institutions

Thomas H. Jackson*

Bankruptcy reorganization is, for the most part, an American success story. It taps into a huge body of law, provides certainty, and has shown an ability to respond to changing circumstances. It follows (for the most part) nonbankruptcy priority rules—"the absolute priority rule"—with useful predictability, sorts out financial failure (too much debt but a viable business) from underlying failure, and shifts ownership to a new group of residual claimants, through the certainty that can be provided by decades of rules and case law.

Notwithstanding its success, bankruptcy reorganization has a patchwork of exceptions, some perhaps more sensible than others.[1] Among them are depository banks (handled by the FDIC), insurance companies (handled by state insurance regulators), and stockbrokers and commodity brokers (relegated to Chapter 7 and to federal regulatory agencies).[2] In recent months, there has been a growing chorus to remove bankruptcy law, and specifically its reorganization process, from "systemically important financial institutions" ("SIFIs"), with a proposed regulatory process substituted instead, run by a designated federal agency, such as the Federal Reserve Board or the Securities and Exchange Commission.

Putting aside political considerations, behind this idea lie several perceived objections to the use of the bankruptcy process. First, it is argued, bankruptcy, because it is focused on the parties before the court, is not able to deal with the impacts of a bankruptcy on other institutions—an issue

---

* Distinguished University Professor, the University of Rochester. Many of the ideas in this paper are a result of stimulating conversations as a part of the Resolution of Failing Tier I Financial Institutions group chaired by Kenneth Scott. I have learned an extraordinary amount from this group's inclusion of me in the process, for which I am very grateful. Errors that remain are mine.

[1] Professor Eisenberg notes that "[h]istorically, bankruptcy law seems to have deferred to some regulatory schemes because those schemes were in place before an extensive federal bankruptcy law was available to corporations," Theodore Eisenberg, *Bankruptcy in the Administrative State*, 50 LAW & CONTEMPORARY PROBLEMS 3, 7-8 (1987).

[2] Michael Sovern, *Section 4 of the Bankruptcy Act: The Excluded Corporations*, 42 MINN. L. REV. 171, 207-29 (1957) (arguing there is less reason to exclude insurance companies than depository banks, and suggesting that if insured depository banks were made subject to bankruptcy, only the FDIC could invoke it and the FDIC would be appointed trustee).

thought to be of dominant importance with respect to SIFIs, where the concern is that the fall of one will bring down others or lead to enormous problems in the nation's financial system.[3] Second, bankruptcy—indeed, *any* judicial process—is thought to be too slow[4] to deal effectively with failures that require virtually instant attention so as to minimize their consequences.[5] Third—and probably related to the first and second objections—even the best-intentioned bankruptcy process is assumed to lack sufficient

[3] There is disagreement about whether there is such a systemic problem. *Compare* Kenneth Ayotte & David Skeel, Jr., *Bankruptcy or Bailouts?*, J. OF CORPORATION LAW (forthcoming 2010), Peter Wallison, "Memorandum for the members of the Pew Task Force on Financial Reform Project" (2009), and Testimony of John Taylor, US House of Representatives, Committee on the Judiciary, Subcommittee on Commercial and Administrative Law, Oct. 22, 2009 (skeptical) *with* Testimony of David Moss, US House of Representatives, Committee on the Judiciary, Subcommittee on Commercial and Administrative Law, Oct. 22, 2009 and Statement of Michael Krimminger, US House of Representatives, Committee on the Judiciary, Subcommittee on Commercial and Administrative Law, Oct. 22, 2009 (a serious problem). Without taking an absolute position on that disagreement—other than to note the central importance of a rigorous definition of both "systemic" and the types of institutions that might raise systemic concerns—the thrust of this paper is to articulate a way in which bankruptcy's reorganization process might be modified so as to address systemic concerns, assuming they are valid. (There is an important question of scope turning on the ability (or not) to predesignate SIFIs, that I discuss *infra* pp. __.) It is widely assumed that bankruptcy's focus on the parties before the court renders it unable to deal effectively with systemic consequences (assuming they exist). *See, e.g.*, Statement of Ben Bernanke, US House of Representatives, Committee on Financial Services, Oct. 1, 2009, at 7 ("the bankruptcy code does not sufficiently protect the public's strong interest in ensuring the orderly resolution of a nonbank financial firm whose failure would pose substantial risks to the financial system and to the economy"); Statement of Michael Krimminger, *supra*, at 6 ("[t]he bankruptcy process focuses on resolving creditor claims and not protection of the broader public interest"); Robert Shiller, "Crisis Averted: What of the Next One?," N.Y. TIMES, Aug. 10, 2008.

[4] This objection, in general, would have had greater saliency in the years immediately following the enactment of the Bankruptcy Code of 1978. In those years, we saw endless extensions of exclusivity periods, as well as significant judicial passivity towards the "debtor in possession" (*i.e.*, usually prebankruptcy management, put in place by the prebankruptcy equity owners), leading to predictable delay—as those "out of the money" always have an incentive to play with other peoples' money. However, over time, it increasingly became the case that judges—and therefore judicial opinions—"got it," and other creative solutions, such as pre-packs and going-concern sales permitted expedition where it was appropriate, all still subject to judicial oversight and to basic rules of the bankruptcy process.

[5] *See, e.g.*, Testimony of David Moss, *supra* note 3, at 1 ("[a]lthough American bankruptcy law has served us extremely well in many different contexts over the past 100-plus years, it was never designed to handle the failure of a large, systemically significant financial institution, particularly at a moment of severe financial turmoil. For one, our bankruptcy procedure may be too slow to deal with the failure of a major financial institution in the midst of a fast moving crisis."). As Professors Ayotte and Skeel note, this objection may be overstated, Kenneth Ayotte & David Skeel, Jr., *supra*, note 3, at 8 ("faced with extreme time pressure, buyers [for Lehman's most valuable assets] materialized, and Lehman quickly sold its viable subsidiaries, allowing them to remain in business under different ownership")—and Lehman is a case complicated in significant ways by the fact that not all of the Lehman entities (such as broker-dealers) could be brought into the reorganization process. They also take issue with the opposite concern—that bankruptcy will lead to a "fire sale," also pointing to Lehman's continuing holding of a significant portfolio of assets more than several months later. *Id.*, at 11. Again, I assume the truth of the objection, so as to fashion a proposal that is responsive to it.

expertise to deal with the complexities of a SIFI and its intersection with the broader financial market.[6]

The premise of my "Chapter 11F" proposal,[7] which I flesh out below, is that, *assuming the validity of each of these objections*, they, neither individually nor collectively, make a case for creating yet another (and very large) exception to the nation's bankruptcy laws and setting up a regulatory system, run by a designated federal agency, that operates outside of the predictability-enhancing constraints of a judicial process.[8] Rather, bankruptcy's process can be modified for SIFIs—my Chapter 11F—to introduce, and protect, systemic concerns, to provide expertise, and to provide speed where it might, in fact, be essential. Along the way, there is probably a parallel need to modify certain other existing bankruptcy exclusions, such as for insurance companies, commodity brokers, stockbrokers, and even depository banks, so that complex, multi-faceted financial institutions can be fully resolved within bankruptcy.[9]

---

[6] *See* Jeffrey Golden, *The Courts, the Financial Crisis and Systemic Risk*, CAPITAL MARKETS LAW JOURNAL, June 6, 2009 and Testimony of David Moss, *supra* note 3, at 7 ("a resolution of these financial firms requires pre-planning and cannot depend on administration by a debtor in possession, a newly appointed trustee, or a creditors' committee"). This concern isn't limited to SIFIs. *See* Theodore Eisenberg, *supra* note 1, at 10 ("[i]f special expertise is needed to assist troubled financial institutions, the bankruptcy court, the traditional bankruptcy forum, may be at a relative disadvantage vis-à-vis federal or state regulatory authorities"). Not everyone agrees that a comparative expertise advantage would lie with an agency designated to "resolve" SIFIs. *See* Peter Wallison, "Pew Task Force," *supra*, note 3; Stephen Haber & F. Scott Kieff, *Wrong Incentives from Financial System Fixes*, in REACTING TO THE SPENDING SPREE: POLICIES WE *CAN* AFFORD (Hoover Institution 2009), at http://ssrn.com.abstract=1496584. Once again, this proposal is presented *assuming* the validity of the objection, so as to fashion an appropriate response to it.

[7] H.R. 3310 (the "Consumer Protection and Regulatory Enhancement Act"), http://thomas.loc.gov/cgi-bin/query/z?c111:H.R.3310: would designate a new Chapter 14 to deal with "Adjustments to the Debts of a Non-Bank Financial Institution." I discuss some of the features of H.R. 3310 in the course of this paper (and, no, I don't care whether the new chapter is called 11F or 14 . . .).

[8] I do not mean to claim that political considerations do not enter bankruptcy, or indeed sometimes can swamp the process. I agree with Professors Roe and Skeel that the use of Section 363 (together with dramatic time constraints and constraints on competing bids) to "sell" Chrysler effectively gutted the priority rules of the reorganization process. Mark Roe & David Skeel, Jr., *Assessing the Chrysler Bankruptcy*, http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1426530; *see also* Barry Adler, Jr., *What's Good for General Motors*, 3 (Annex A to Congressional Oversight Panel, September 2009), at http://cop.senate.gov/documents/cop-090909-report.pdf) (the Chrysler bankruptcy provisions "illegitimately distributed assets inconsistently with the priorities established under the Bankruptcy Code"). But to recognize that a judicial process is not perfect, is not to say that it cannot perform better, or with greater certainty, than a non-bankruptcy "resolution" process handled by a designated government agency, where political considerations are almost certain to invade financial decisions. *See* Peter Wallison, "The Meaning of the Lehman Bankruptcy," before The American Bankruptcy Institute (Nov. 5, 2009), *American Enterprise Institute for Public Policy Research*.

[9] *See generally* David Skeel, Jr., *Bankruptcy Boundary Games*, http://ssrn.com/abstract=1446762, at 5 ("[w]ith the benefit of twenty-twenty hindsight, we can see that the brokerage exclusion was designed with the brokerages of the 1960s particularly in view"); David Skeel, Jr., *The Law and Finance of Bank and Insurance Insolvency Regulation*, 76 TEX. L. REV. 723 (1998) (banks, probably no; insurance companies,

If we seek, as George Shultz has counseled us, ways to make failure tolerable, we need to allow failure, and to have the consequences of that failure fall on the parties who had contracted *ex ante* to bear the risks of such failure according to predictable rules. Bankruptcy, I would argue, performs precisely this function, and the objections to it that lead to another set of exceptions simply do not make the case for eliminating bankruptcy, rather than taking it and, with changes, working within its structure.[10] Can bankruptcy, even if revised along the lines I propose here, eliminate bailouts? Probably not, for the government can always intervene. But a system of established rules, judicial oversight (including appeals to Article 3 courts), and full public disclosure, has a better chance of both reducing bailouts—and making the costs of them known—than does a nonbankruptcy resolution authority. The predictability of bankruptcy helps ensure, *ex post*, that risks remain where they belong, which will aid, *ex ante*, appropriate risk-taking activities as well as monitoring by those exposed to potential losses in any resulting bankruptcy.[11]

Before setting forth the proposal itself, there is one other important background question that involves the scope of any new Chapter 11F. The workshop for which this paper was prepared focused on systemically important financial institutions, and this paper originally focused exclusively on that category. I am in complete agreement with John Taylor's contribution to that workshop,[12] which suggests that we don't have a focused or coherent definition of systemic risk, and with the observation that it is difficult, indeed imprudent, to recommend a policy change limited to SIFIs without knowing precisely what they are.

Moreover, as I thought about it—and here my views may well diverge from other workshop contributors—the category of "systemic" is limited, un-

---

probably yes); Kimberly Summe, "Making Failure Tolerable: Addressing the Derivatives and Repo Markets," Workshop Paper Dec. 11, 2009, at 11 ("True progress will be made when our bankruptcy regime reflects the diverse nature of contemporary financial groups. In order to ensure that future failures of systemically important entities are tolerable for the financial system, a unified bankruptcy approach must be adopted.").

[10] *See, e.g.*, Testimony of Harvey Miller, US House of Representatives, Committee on the Judiciary, Subcommittee on Commercial and Administrative Law, Oct. 22, 2009, at 3 ("[n]o rationale is given for why the existing bankruptcy law and bankruptcy courts could not deal with the resolution of such financial crises, provided that the bankruptcy code is amended to restore the applicability of the bankruptcy code's automatic stay to derivatives, swaps and other securities transactions").

[11] This point is made very nicely in Richard Herring's contribution to this conference, "Proposals for Wind Down Plans," Workshop Paper Dec. 11, 2009.

[12] John Taylor, "Defining Systemic Risk Operationally," Workshop Paper Dec. 11, 2009.

likely to occur often outside of depository bank "runs," and almost impossible to predict in advance. Let me explain by a brief detour to thinking about the issue outside of the context of financial institutions. In Chrysler—hardly the largest "American" (whatever that might mean) automobile manufacturer—much of the plan of reorganization, and the "need for speed," was premised on the repercussions that would occur to the American economy, its jobs, and its communities, if Chrysler were allowed to liquidate.[13] First of all, I think of these as *direct* not *systemic* consequences, and—even then—they would have been not consequences so much of a Chrysler bankruptcy as of an overcapacity problem in the automotive industry. They are "direct" because they are all caused by known, contractual, linkages to Chrysler. It is known, and predictable, what will happen to a dealer if Chrysler liquidates. Likewise, the effects on a Chrysler supplier are also known and predictable. The consequences might be large, but they aren't, therefore, necessarily systemic—any more than they would be if Chrysler were fully vertically integrated and thus owned both suppliers and dealers.[14] Moreover, they aren't even a consequence of a Chrysler liquidation so much as a consequence of overcapacity in the automotive industry. An industry scaled to produce 17 million cars that needs to scale back to something smaller—whether 12 million or 14 million or some other number doesn't really matter—has to face the wrenching consequences of that, in terms of lost jobs, shuttered plants, and effects on sup-

---

[13] Declaration of Thomas J. LaSorda, April 30, 2009, at 3-4 (Docket # 51, linked to through www.chryslerrestructuring.com):

> Should Chrysler liquidate, the reverberations throughout the American economy (and NAFTA economies generally) will be severe in both breadth and depth. A Chrysler bankruptcy would mean the immediate loss of 38,500 Chrysler jobs in the United States—including 27,600 union members—and 55,000 Chrysler jobs worldwide. Chrysler's workers and retirees and their surviving spouses will lose over $9.8 billion in health care and other benefits as well as $2 billion in annual pension payments. Chrysler's annual cash payments of nearly one billion dollars per year to over 106,000 retirees will disappear. Twenty-three Chrysler manufacturing facilities and 20 parts depots in the United States will close immediately. Chrysler's $35 billion dollars in annual automotive supplier payments will evaporate, bankrupting many of these suppliers. Indeed, over $5.3 billion currently owed to automotive suppliers will go unpaid. The effects on dealers will be similarly far-reaching—over 3,200 dealers would close, taking with them 140,000 jobs—and the dealers' local communities will likely lose $100 billion in annual sales. Moreover, the 31 million owners of Chrysler automobiles will see their vehicles lose their warranties, and their ability to get parts and service for the cars, which will translate to a significant loss in their value.

These ideas were repeated throughout the Chrysler papers and proceedings.

[14] I leave open the question as to whether such a firm might ever be "so large," in terms of its own size and direct consequences, to be considered "systemic." My intuition is "no," because in a world in which *no* entity should be "too big to fail," the players to this failed enterprise can all be dealt with in an existing bankruptcy proceeding. The government might want to deal with the consequences of the failure, such as in job retraining programs, but it does not need to be "represented" in the proceedings of the failed company so as to "represent" interests not otherwise adequately represented. Bankruptcy's structure was up to the task of reorganizing (or liquidating) Chrysler and GM; the abuse of the process in order to achieve government bailout goals will, I think (or hope), come to be recognized as a sad failure of bankruptcy's rules and the judicial oversight process. *See* Mark Roe & David Skeel, Jr., *supra*, note 8; Barry Adler, Jr., *supra* note 8.

pliers. In that world, Chrysler, as one of—if not the—least efficient producers *should* be the one who takes the most serious "hit" from this reality. Treating the consequences of a Chrysler liquidation as making it "too big to fail," as the government seemed to do, only implies that the effects of overcapacity will not be allowed to fall on the inefficient, but will be "spread" throughout the automotive manufactures more broadly. In other words, the efficient will be required to suffer so that jobs can be "saved." Not a very good policy, in my view.[15]

What does this have to do with financial institutions? The case for treating them as "too big to fail" isn't a result of the number of jobs, or suppliers, or dealers; rather it is because of the potentially broader effects on the economy that aren't measured by the financial institution's failure itself. But I think it is still useful to consider, by analogy, a manufacturing company such as Chrysler. If the size of its operations—jobs, plants, suppliers, etc.—aren't enough to treat its consequences as anything other than "direct," then what might "systemic" consequences be? They would be, in my view, most clearly a category of consequences visited on others not directly linked to Chrysler—John Taylor's "indirect" category.[16] As with a "run" on a bank spilling over to other banks, it would be what would happen if a Chrysler liquidation were to lead automotive buyers to decide there was something unsound about buying a car (and not just a Chrysler), and they were to stop buying GM, Ford (and Toyota and Hyundai) cars as well. *That* would be systemic—but it would also be almost impossible to predict in advance.

So, too, in the area of financial institutions. While the failure of depository banks may "spread" systemically (with the "triggering" institution, parenthetically, not necessarily "large"—thus there is an incorrect conflating of SIFI with "bigness" if one focuses on these indirect consequences),[17] it is rather hard to figure out, particularly in advance, where else such "runs" might occur. Thus, I am sympathetic to the observation Peter Wallison made in commenting on my paper at the workshop that, outside of depository banks, he is skeptical there are systemic financial institutions. Or—I might add—even if there are, we won't know them (or be able to define them) until such a "run" occurs. To be sure, financial institutions aren't manufacturing

---

[15] This is one of the general problems with "bailouts"; they not only distort *ex ante* bargains (and attendant monitoring), they also interfere with natural readjustment processes. Responding to an overcapacity problem by trying to "save jobs," is tantamount to a decision to save inefficient players, rather than deal directly—through retraining and other possible interventions on those who lose jobs—with the consequences.

[16] John Taylor, *supra* note 12.

[17] Perhaps the catch-phrase should be "too systemic to fail" rather than "too big to fail."

institutions, and the effects on the economy might be viewed as "systemic" without being viewed as "indirect."[18] But my sense is one of caution—which only adds to the definitional difficulty that John Taylor has so cogently pointed out.

This leads me to the notion that my proposals can—and perhaps should—be considered as proposals for *all* financial institutions, not just SIFIs.[19] Remember my premise: I'm responding to the idea that there may be "systemic" effects that others think bankruptcy cannot handle. I'm attempting to "merge" that premise with the reality that such systemic effects may be so hard to predetermine that a cogent category of predesignated SIFIs may be unwise, if not impossible. If we cannot predesignate, then I favor the consideration of the availability of Chapter 11F for all financial institutions. To be sure, if there aren't systemic consequences, then worrying about the impact of bankruptcy on parties not directly involved in the bankruptcy proceeding may be unnecessary, and some of the proposals will be superfluous. But superfluous does not mean unworkable. It would be up for the bankruptcy court (restructured as I propose) to decide when and how, within the bankruptcy process, to involve the procedures specifically focused on systemic consequences. Alternatively, if there is indeed a workable definition of what is a SIFI that emerges that permits predesignation, it could be used so as to limit my proposals to SIFIs alone. My point is only that consideration of the use of making bankruptcy *the* resolution mechanism for SIFIs does not need to await a consensus definition of a SIFI.

So, here goes. What follows is the outline of ways in which I would envision the current provisions of Chapter 11 being modified or eliminated, in order to provide a viable bankruptcy vehicle for the resolution of financial institutions (or, if we can agree on a definition to be applied in advance, SIFIs).[20]

---

[18] For example, vertical integration wouldn't necessarily encompass counterparties and their dealings with a financial institution. Even so, these *are* contractual relations, whose risks are known in advance. And, as a note of factual caution, Lehman's failure did not result in the failure of any of Lehman's counterparties. Peter Wallison, Comments on Thomas Jackson, "Chapter 11F," Workshop of December 11, 2009. But if it had, would those results be "systemic"? I remain skeptical, but there are perhaps reasons to treat them as "systemic" when we might not treat the failure of a supplier to Chrysler in a similar fashion.

[19] To be sure, we may well have some definitional ambiguity over what is a "financial institution" just as we have over what is "systemically important." But I will assume, as I think the entire workshop has, that the difficult issues are not those of what are "financial institutions" but what are "systemically important." As I will discuss later, the current FDIC regime for depository banks could be left in place for depository banks that are not a part of (*i.e.*, a subsidiary of) a larger financial institution.

[20] My bankruptcy proposal is easily seen as in parallel, rather than in conflict, with proposals such as Darrell Duffie's contribution to this conference, "A Contractual Approach to Restructuring Financial Institutions," as there will still potentially be cases where the contractual methods don't work, and bankruptcy (or insolvency) results. Similarly, Richard Herring's contribution to this conference, *supra* note 11,

- **Use existing Chapter 11 (or Chapter 7) procedures, modified as proposed below—probably in a new chapter or subchapter (which I will call "Chapter 11F").**

Explanation Throughout, I am attempting to capture the "good" features of the bankruptcy reorganization process, while being responsive to some of the concerns—addressing systemic concerns beyond the debtor and its immediate claimants, expertise, and speed—that have led to a resistance to consider the bankruptcy process as a viable one for the resolution of SIFIs.[21]

Perhaps here, more than anywhere, there seems to be a deep divide between those whose primary focus is bankruptcy and those whose primary focus is financial institutions or financial instruments.[22] Of course, I come at this from the bankruptcy side, but I do find, historically, claims of the necessity of an "exception" to bankruptcy to be overbroad. Oftentimes, the first reaction of people to a "new" crisis is that bankruptcy isn't up to the task, or that existing nonbankruptcy agencies are better suited. Thus, we already have significant exceptions: Not just depository banks, but insurance companies, and commodity and securities brokers (at least in terms of Chapter 11). Few of these exceptions withstand detailed scrutiny.[23] The "first" Chrysler rescue from 1979 was driven, in significant part, by a fear that an automotive company could not survive bankruptcy reorganization because of loss of consumer confidence.[24] There was a large consensus around this point, and the

---

involving the mandatory adoption of wind-down plans, would, I would think, facilitate a bankruptcy resolution such as I am proposing here.

[21] Certain concerns—most particularly, speed—could be significantly aided by a proposal such as Richard Herring's, *see* Richard Herrring, "Proposals for Wind Down Plans," *supra* note 11. Even if not able to forecast every detail in advance, as Joseph Grundfest cautions in "Wind Down Plans in Practice: The Prenup Analogy," they would almost certainly provide a wealth of information and background thinking that would be extraordinarily useful in a bankruptcy proceeding.

[22] *Compare* Testimony of Harvey Miller, *supra*, note 10 and Kenneth Ayotte & David Skeel, Jr., *supra*, note 3, *with* Testimony of David Moss, *supra*, note 3 and Remarks by FDIC Chairman Sheila Bair to the Exchequer Club of Washington D.C., June 18, 2008 ("I believe that we need a special receivership process for investment banks that is outside the bankruptcy process, just as it is for commercial banks and thrifts. The reason goes back to the public versus private interest. The bankruptcy process focuses on protecting creditors. When the public interest is at stake, as it would be here, we need a process to protect it."). *See also* Peter Wallison, "Pew Task Force," *supra*, note 3 (arguing for the preferability of bankruptcy over a government resolution process).

[23] Michael Sovern, *supra* note 2; David Skeel, Jr., *The Law and Finance of Bank and Insurance Insolvency Regulation*, *supra* note 9.

[24] *See* R. REICH & J. DONAHUE, NEW DEALS: THE CHRYSLER REVIVAL AND THE AMERICAN SYSTEM 106, 102-12 (1985).

events of the past 30 years have shown it to be completely wrong. We have reorganized dozens of large manufacturing, retail, and service businesses with almost no one not intimately involved in the proceedings even noticing. People continued to fly on United when it was in bankruptcy. People continued to shop at K-Mart and eat at Ponderosa and Bonanza steakhouses when they were in bankruptcy. People continued to buy suits made by Hartmax and its subsidiaries when it was in bankruptcy. But expensive durables we were, told, are different, because of warranty concerns. And then Chrysler, followed by GM, actually used bankruptcy (even though we were told that GM's board never even drafted contingency plans since bankruptcy wasn't a viable option) and, in terms of customer reaction, almost nothing happened.[25] Whatever defects of the recent restructuring of Chrysler and GM through bankruptcy, it is clear that the idea that filing for a bankruptcy reorganization would inevitably lead to liquidation was overstated. Similarly, the 1980s saw a concern about utility companies using bankruptcy—concerns that were also wildly off the mark.[26] Thus, I think the first reaction—bankruptcy isn't up to the task of handling large financial institutions—isn't necessarily the right reaction. I think we owe a serious look at bankruptcy's viability in terms of SIFIs before we rush to create another exception that may, later, lead to its own set of complexities, as the exceptions for commodity brokers and stockbrokers in Chapter 11 arguably did in the Lehman bankruptcy.

- **[Optional] A discrete and limited set of institutions are pre-designated by appropriate government agencies/officials as SIFIs, thereby making them automatically eligible for Chapter 11F.**

Explanation As I discussed earlier, *if* we can agree on a useful definition of what makes a SIFI a SIFI (as opposed to an "ordinary" financial institution), then this Chapter 11F proposal could be limited to such institutions. The linkage between the ability to define a SIFI and implementing Chapter 11F limited to them is, in my view, tight. Without a pre-designation, and if Chapter 11F were otherwise limited to SIFIs, starting an appropriate bankruptcy proceeding is made more complex, as it will not be immediately clear whether the entity is subject to Chapter 11 or to Chapter 11F. There are enough distinct features, explored below, including some that are immediately relevant, so that pre-designation is superior to an early determination within bankruptcy. (While a government agency can—as I suggest below—be given the

---

[25] Albeit, warranties were assumed, as they almost surely needed to be; Chrysler, however, did *not* assume non-warranty products liability claims.

[26] *See* Theodore Eisenberg, *supra*, note 1.

power to commence a bankruptcy proceeding against a SIFI, thus giving rise to the possibility of a contemporaneous, rather than advance designation, that would work only for government-commenced bankruptcy proceedings. Traditional voluntary and involuntary proceedings would require a "sorting out" period, with its attendant complications.) Thus, my proposal is for Chapter 11F to be available to any financial institution[27] unless a satisfactory definition of a SIFI that would permit pre-designation were to emerge, in which case it would be feasible, and perhaps politically more palatable, to limit its scope to SIFIs.

- **The relevant government agency (*e.g.*, FRB, FDIC or SEC [one, not all]) is given the power to file an involuntary petition with respect to a financial institution directly into Chapter 11F.**

Explanation The Bankruptcy Code depends on a debtor, or its creditors, to initiate bankruptcy proceedings. That's wholly appropriate for a system in which the only "relevant" interests are represented by claimants against the debtor. In the case of a SIFI, however, where there is an argument or worry about a systemic event affecting other institutions, the appropriate government agency should be able to file a bankruptcy proceeding directly in Chapter 11F. (Since I am assuming we cannot predetermine the financial institutions that are significantly important, this power would necessarily exist with respect over all financial institutions.) This is an effort to reproduce some of the "power" of the relevant government agency in proposals for giving such an agency "resolution authority" outside of bankruptcy, but requiring it to be exercised within the judicial framework of a bankruptcy proceeding.[28]

- **Should the relevant government agency take specified steps that amount to a non-bankruptcy resolution of a financial institution, three or more creditors may commence a bankruptcy case under Chapter 11F for that entity, and the agency's steps will constitute grounds for an "order for relief" under §303(h) of the Bankruptcy Code.**

Explanation In an involuntary case, the "commencement of the case" is distinct from the "order for relief," the latter being specified in §303(h) as fol-

[27] Apart from, perhaps, depository banks not themselves a part of a larger financial organization, which might continue to be resolved under existing FDIC procedures.

[28] A similar provision is in Barney Frank's "Discussion Draft" of October 27, 2009 (Section 1105 "Authority to File Involuntary Petition for Bankruptcy").

lowing from a demonstration (1) that "the debtor is generally not paying such debtor's debts as such debts become due" or (2) "a custodian . . . was appointed or took possession." This proposal would treat the efforts at a resolution by the relevant government agency as a third ground for an order for relief (perhaps comparable to the idea of the appointment of a custodian). This is an attempt, perhaps symmetrical with the prior provision, to limit end-runs around bankruptcy by a government-engineered bailout that is not subject to the rules and judicial oversight of a bankruptcy proceeding. It may not be wholly successful—one may not know (for example) if the government is engaging in such steps (indeed, it might encourage efforts at government secrecy), and it may be difficult to adequately define (and limit) the events that constitute an end-run nonbankruptcy resolution. Still, it seems to me to be a crucial feature to focus on resolution by bankruptcy rather than "bailout."

Alternative Proposals H.R. 3310 provides, in proposed Sec. 1403, for a ten-day period (that can, on motion, be shortened, or extended for 30 additional days—although that extension is post-petition) before a bankruptcy petition may be filed in which a non-bank financial institution (the entities subject to proposed Chapter 14) must participate in "prepetition consultation in order to attempt to avoid the need for the non-bank financial institution's liquidation or reorganization in bankruptcy, to make any liquidation or reorganization of the non-bank financial institution under this title more orderly, or to aid in the nonbankruptcy resolution of any of the non-bank financial institution's components under its nonbankruptcy insolvency regime." In a similar fashion, a proposal submitted by Robert Eager would provide for a 30-day period (extendible by the Treasury) for the appropriate federal regulatory agency to "manage the potential financial crisis," before court review would commence.[29] I am unconvinced that the idea that there should be some period of time to attempt "resolution" of a financial institution outside of the judicial framework that is, ultimately, one of the principal advantages of a bankruptcy resolution process, is a good one. Such a judicial framework has established rules, including priority rules, and has the best chance of separating out issues of resolution and responding to systemic concerns, on the one hand, and bailout on the other hand.

- **In Chapter 11F, existing bankruptcy exclusions for depository banks, insurance companies, stockbrokers, commodity brokers, and the like, see**

[29] Robert Eager, "Recommendation Regarding Resolution Authority for Systemically Significant Financial Institutions," October 5, 2009.

Bankruptcy Code §§ 109(b)(2), (b)(3), (d), would not apply, so that the "entire" financial institution could be "resolved" (reorganized) within the context of a single bankruptcy proceeding.

Explanation Whatever the justifications for the current exclusions from the Bankruptcy Code (and I'm inclined to think there aren't many, except perhaps for the regime of depository banks), those exclusions create needless complexity, and interfere with successful resolution, of complex financial institutions. Because of cross-guarantees, and the often vast proliferation of separate operating entities, trying to "resolve" one part of a complex financial institution, with other parts being dealt with by other regimes, is problematic at best, and likely detrimental. (Creative lawyering circumvented many of the problems of the exclusion of brokerages in the Lehman bankruptcy, and I can only imagine the complexities that would have been introduced by the exclusion of insurance companies if AIG had, in fact, been allowed to fail.[30]) (The bankruptcy doctrine of "substantive consolidation" may be appropriate in cases involving significant cross-guarantees, but only applies if all the entities are subject to bankruptcy jurisdiction.) Likely the most controversial aspect would be the inclusion of depository banks, to the extent that they were a part of a broader financial institution's "empire." In this limited category of institutions, however, I think it is better to effectively duplicate the FDIC's powers and processes over the depository-features of such banks within a broader bankruptcy proceeding, than to have some parts of the financial institution "resolved" within bankruptcy and other parts "resolved" by the FDIC, outside of bankruptcy. (Such would not be the case for depository institutions not themselves a part of a broader financial institution network; those institutions could continue to be resolved by the FDIC outside of bankruptcy.) Similarly, for brokerages, the appropriate Chapter 7 provisions, §§ 741 – 753, could be used, where appropriate, as a baseline for those parts of a complex financial institution within a Chapter 11F proceeding. Without something such as this, serious conflicts among different resolution authorities would remain not just possible, but likely.[31]

---

[30] As of 2007, AIG "was ranked the largest life insurer and the second largest property/casualty insurer by premiums written in the United States," and "is supervised in the United States by a host of state insurance regulators," Report of Neil Barofsky, Factors Affecting Efforts to Limit Payments to AIG Counterparties," SIGTARP Report. 10-003 (Nov. 17, 2009), at 2-3 & n. 7.

[31] *See, e.g.*, Kimberly Summe, "Making Failure Tolerable," *supra* note 9, at 10-11 ("there are no systemically important entities . . . that conduct the significant majority of their derivative business out of an identified financial holding company" and thus "the Obama Administration has missed a unique opportunity to address the economic and procedural inefficiencies produced by our fragmented bankruptcy regime. . . . . True progress will be made when our bankruptcy regime reflects the diverse nature of contemporary financial groups") ; see also *id.*, at 3 ("the three largest derivatives portfolios are now held by the United States' three largest bank holding companies").

Alternative Proposals Paul Volker has proposed separating depository banks (*i.e.*, deposit taking and loan-making) from trading operations and other financial services. Such a proposal would, if implemented to prohibit even parent-sub relationships, ensure that a depository bank would never be a SIFI, and thus the current FDIC regime could continue. I view my proposal as less radical and disruptive of existing institutions. (Although, if it is thought that quick transfer of guaranteed deposits to a third-party is essential to preventing "runs" or other social goals—I am not convinced it is anymore—then some variant of Volker's proposal may be useful to consider. Given that the FDIC transfers (naturally) assets as well as (depository) liabilities, both a quick assessment of assets and the quick ability to transfer them necessarily follow. The more complex the depository bank, the more this seems inevitably to remove this process from salutary judicial oversight. Restrictions on types of risky assets and on cross-guarantees of depository banks—even when a part of a broader SIFI ownership structure, may be a necessary corollary of meshing the FDIC's role over guaranteed deposits with the bankruptcy goal of judicial oversight and treatment predictability.) Again, the loss to the FDIC's jurisdiction is more theoretical than real, as many of the rights and responsibilities of the FDIC over the depository features of such banks could be duplicated within the bankruptcy proceeding—and depository banks that are not part of a broader financial institution could, without significant disruption, simply be left outside of bankruptcy under FDIC jurisdiction.

- **Upon the commencement of a Chapter 11F case, it will be assigned by the Chief Judge of the relevant Court of Appeals to a member from a previously designated (by the relevant government agency) panel of special masters.**

Explanation The idea here is to try to get someone with relevant expertise, which a randomly-assigned bankruptcy judge may very likely not have. Ideally, one could imagine specially-selected experts—a pre-selected group of "special masters" (who have expertise both in the fields of financial institutions and bankruptcy law)—to whom these cases could be assigned. (As bankruptcy judges are not Article 3 judges, these "special masters" could presumably handle everything that a bankruptcy judge is currently able to handle without tripping into the concerns of their lack of constitutional Article 3 status. Technically, the "assignment" is through a district judge; I am ignoring this complexity for purposes of exposition.) They would be paid by the government, at pre-arranged rates, and, like special masters appointed by the Supreme Court, would have authority to hire additional staff, including

experts.[32] There would be an issue of the ability of these special masters to "drop everything" and take on a quick-moving SIFI bankruptcy resolution, although I think that is manageable. Indeed, both for purposes of expertise and speed, it would be possible to imagine a "panel" of special masters appointed to oversee the reorganization (or resolution) of a particularly complex financial institution.

- **With respect to Qualified Financial Contracts (QFCs), (a) there would be no automatic stay (or related call-off of bankruptcy-specific provisions) for any QFCs for which the financial institution's security was "cash" (or "cash-like"—narrowly defined) collateral, and (b) for all other QFCs of the financial institution, the traditional provisions of the Bankruptcy Code, including the automatic stay, would apply unless and until lifted by court order.**

Explanation This attempts to weave a line between the current system (first, setoffs pursuant to QFCs against "property held by, pledged to, under the control of, or due from" the counterparty are not subject to the automatic stay, *see* Bankruptcy Code §§ 362(b)(6), (7), (17) & (27), second, the counterparties can terminate a QFC for "ipso facto" reasons of a sort described in Bankruptcy Code § 365(e)(1), *see* Bankruptcy Code §§ 555, 556, 559, 560, and 561, and, third, preference law (particularly) with respect to margin or settlement payments—or comparable QFC transfers—made to counterparties, is likewise called off, *see* Bankruptcy Code § 546(e), (f), (g), (j)) and simply moving to a system where they, like other claims, are subject to the automatic stay (and other bankruptcy provisions) for (and before—such as in the case of preferences) the duration.

It is important to note what these provisions do—and do not do—for QFCs. As has been pointed out elsewhere: "Contracts that are financial in nature are treated differently than garden variety executor contracts even if they do not qualify for the safe harbor treatment. Loans and other monetary obligations accelerate as of the date of the bankruptcy filing [Bankruptcy Code § 502(b)]. Financial accommodations contracts are not assumable and assignable by a bankrupt debtor [Bankruptcy Code § 365(c)] and bankruptcy termination clauses in these contracts are enforceable [Bankruptcy Code

[32] I don't see these as full-time judges, as we hope there wouldn't be sufficient work—which is also a defect of any proposal to create (by analogy to the federal court of appeals for patents) a special "court" for financial institutions; the judges (hopefully) would spend much of their time with nothing to do. This might be somewhat less the case if Chapter 11F applied to all financial institutions, rather than just SIFIs, and might justify a single court staffed with several "experts" as judges. Even there, the advantage of the special master system may be in allowing a level of pay to actually bring forth individuals with the necessary expertise, who may not be willing to toil, full-time, at a bankruptcy judge's salary.

§ 365(e)]. In addition, while setoff generally is subject to the automatic stay, recoupment is not. Thus, other than the right to foreclose on posted collateral, which right is useful in practice only when the non-debtor counterparty has actual possession of the collateral, the special protections granted to the safe harbor contracts do not appear to be so special."[33] (I'd add to this list of "special" treatment of QFCs the ability to exempt settlement and margin payments—and other QFC-related transfers—from the trustee's avoiding powers under Bankruptcy Code § 546(e), (f), (g), and (j).)

I propose a two part system. In the first part, for repos and other QFCs backed by "cash-like" collateral (to be pre-defined, in a rather limited fashion), the existing provisions—which call off the Bankruptcy Code's automatic stay as applied to setoffs, prohibition on the enforcement of ipso facto clauses, and preference provisions—would continue in force. (Bankruptcy—as it does now—would relieve the financial institution from continuing obligations to post new collateral on the QFCs, as it retains the right to reject the underlying contract (even if the counterparty doesn't terminate it[34]), see Bankruptcy Code § 562; essentially, the current Bankruptcy Code rules regarding QFCs would allow the counterparty to take steps to terminate the contracts, access existing collateral in its possession, and protect the counterparty from otherwise preference-like payments within the 90 days before bankruptcy.) The rationale for this is that cash-like collateral is less likely to have a "going concern value" separate from the value of the collateral, and the important expectations of counterparties regarding access to cash collateral—at least a major part of the original rationale for excepting QFCs from the automatic stay (and related bankruptcy proceedings)—trump the costs to the financial institution by permitting the immediate termination of such cash-like collateral-backed QFCs. If there are systemic effects—beyond just allocating the significant costs of failure itself—it is most likely to be felt by the freezing in place of extremely liquid assets that, in normal times, are expected to move from entity to entity at a moment's notice.

---

[33] Shmuel Vasser & Matthew Kerfoot, "Preferential Treatment of Derivative Contracts—Savior or Scourge?," Paper Presented at the American Bankruptcy Institute's 2009 Legislative Symposium, Nov. 16-17, 2009)), at 5-6.

[34] Indeed, there is a strong argument—by analogy to financial accommodation contracts—to treat QFCs as terminated upon bankruptcy, so that rights and liabilities are fixed as of that time, and also neither assumable nor assignable by the debtor (with perhaps an exception for those involved with FDIC-controlled depository banks that might be assigned as a part of the depository bank resolution process within Chapter 11F). *Cf.* Kimberly Summe's discussion, "Making Failure Tolerable," *supra* note 9, of *In re Lehman Brothers Holdings Inc.*, Case 08-13555 (Bankr. SDNY Sept. 15, 2009) ("Metavante") ("The Congressional history behind the safe harbor provisions indicated to Judge Peck that it was the intent that swap market participants would immediately, or at least 'fairly contemporaneously', terminate qualified financial contracts . . .").

In the second part—*i.e.*, for all other QFCs—the existing special provisions would be rescinded, subjecting these QFCs to the ordinary provisions of the Bankruptcy Code, including the automatic stay, non-enforcement of ipso facto clauses, and applicability of preference law. Except for QFCs that might, as is the case now, be assigned by authorization of a relevant government agency to a third-party in conjunction with its assigned role over deposits or other such things, these QFCs, like other financial accommodations, would be deemed "rejected" in bankruptcy, with damages fixed "as of the date of the filing of the petition" under Bankruptcy Code § 502(b) and the non-debtor counterparty would have rights in collateral posted to the QFC as of that date as well. This would help ensure, as Richard Herring notes in his contribution to this conference, that "sophisticated counterparties" that are often in "the best position to monitor and exercise market discipline," in fact *do* that monitoring.[35] I am not denying the possibility of systemic effects as much as saying that here the first-order issue seems to me to be the allocation of losses to those, *ex ante*, who bargained for them, rather than shifting them to others. With respect to such claims, bankruptcy both freezes the value and the movement of additional collateral at the moment of bankruptcy, which appropriately signals the counterparties the extent to which they need to cope with the resulting losses. That potential, known in advance, both reduces the moral hazard (too frequent reliance on non-cash-like backed QFCs) *and* the inattention of the counterparties to worsening financial signals by the financial institution that undermines healthy monitoring.

Alternative Proposals H.R. 3310 is doing something with respect to QFCs and the automatic stay but, with deference, it is almost impossible to figure out quite what. (a) Proposed Section 1401 provides that "[e]xcept as provided in section 1408 [a provision providing for conversion to Chapter 7], sections 362(b)(6), 362(b)(7), 559, 560, and 561 do not apply in a case under this chapter." This seems designed to remove the exception from the automatic stay for QFCs in the case of Chapter 14. Unfortunately, however, by failing to call off various other Bankruptcy Code provisions, notably §§ 362(b)(17) & (27), 555, and 556, it is unclear whether this effort would fully succeed. (In addition, Section 1401 is silent about the continued effect of Bankruptcy Code § 546(e), dealing with the inability to use avoiding powers with respect to margin or settlement payments.) (b) This could be clarified by more precise drafting but, unfortunately, the provisions of proposed Section 1407 cast doubt on the intention of proposed Section 1401. Proposed Section 1407 provides that "upon motion of the debtor, consented to by the Market Stability and Capital Adequacy Board—(A) the debtor and the estate shall be exempt from the operation of sections 362(b)(6), 362(b)(7), 559, 560, and 561 . . . ."

[35] Richard Herring, *Proposals for Wind Down Plans*, *supra* note 11.

These, however, are precisely the provisions referenced in Section 1401, which has *already*—and automatically—exempted the debtor and the estate from the operation of these provisions. In short, proposed Section 1401 seems (subject to some drafting awkwardness) to subject QFCs to the automatic stay from the get-go, while Section 1407 seems to assume that QFC are *not* subject to the automatic stay except upon the approval of a motion. Drawing on the experience of Lehman, Harvey Miller has proposed simply eliminating the exceptions that QFCs have come to enjoy from the operation of the automatic stay.[36] David Skeel has made several proposals, including distinguishing between types of QFCs (*e.g.*, repos would continue their exemptions but not credit default swaps—an idea comparable to my "cash collateral" distinction), but focuses most particularly, as would be relevant to a special bankruptcy chapter for SIFIs, on removing the exemption of QFCs from the automatic stay for SIFIs.[37] My proposal is an intermediate one—to try to disentangle systemic concerns from negative consequences of having an exemption from the stay, as evidenced by Lehman. Alternatively, one could design a system in which the first part of my proposal were adopted—QFCs with "cash collateral" would not be subject to the automatic stay (and related bankruptcy provisions) and other QFCs would be subject to a very short stay (such as one business day), during which time the relevant government agency could arrange their transfer to a third party. Although closest to the existing mechanism used by the FDIC to resolve depository banks, I ultimately disfavor this as (a) too complex, (b) too difficult to accomplish without simply waiving judicial oversight, and (c) too favorable to this particular category of counterparties. Moreover, it introduces some uncertainty into the system, which is a cost over a solution that simply reverses the exemption from the automatic stay entirely in Chapter 11F.[38] *Ex ante*, there may be fewer such QFCs (and more monitoring), but I see this as a *consequence* more than a *cost*.

- **The relevant government agency is given special standing in Chapter 11F (I'm thinking here—loosely—of the idea of a US Trustee or perhaps the role (amplified) of the Commodity Futures Trading Commission under §762)—as a way of getting expertise into the system. In the case of the**

[36] Testimony of Harvey Miller, *supra*, at note 10 ("[t]his caused a massive destruction of value for Lehman. As of September 15, 2008, the bankruptcy date, Lehman's derivative counterparties number approximately 930,000, of which approximately 733,000 sought to terminate their contracts").

[37] David Skeel, Jr., *Bankruptcy Boundary Games*, *supra*, note 9, at 24 & 28. That assumes, of course, that we can effectively pre-designate SIFIs.

[38] *Cf.* Edward Morrison & Joerg Riegel, *Financial Contracts and the New Bankruptcy Code: Insulating Markets from Bankruptcy Debtors and Bankruptcy Judges*, 13 AM. BANKR. INST. L. REV. 641 (2005).

FDIC, its role over the resolution of the depository-specific features of banks would be embodied within the bankruptcy proceeding to the extent feasible—but they would be in coordination with, and under the ultimate control of, the bankruptcy court, rather than separate from (as is the case today).

Explanation As with the idea of an "expert" special master, this is a way to try to get expertise into the system, but have the expertise be subject to a neutral (albeit informed) decisionmaker. In a way, this tries to accomplish, wholly within bankruptcy, the idea of judicial oversight that is (in my view) introduced awkwardly in Robert Eager, where it only comes into play after "a 30-day exclusive period during which [the regulatory agency] can take actions without immediate judicial oversight."[39] The US Trustee analogy is only meant to be suggestive; the actual role for the appropriate government agency should be spelled out in some detail.

- **Eliminate the exclusivity period for the filing of a plan of reorganization provided to the debtor under Bankruptcy Code § 1121(b) and provide that the relevant government agency is one of the entities permitted to file a plan of reorganization.**

Explanation In the typical Chapter 11 case, the Bankruptcy Code provides that "only the debtor may file a plan until after 120 days after the date of the order for relief under this chapter," § 1121(b). Given both the likely need for speed—although some of that might be accomplished by sales under Bankruptcy Code §363 with appropriate safeguards of claimants—and the concern over systemic issues that a debtor will not internalize, it should be clear that there is no exclusivity period and that the relevant government agency can file its own plan, subject to meeting the substantive and procedural requirements of the Bankruptcy Code.

- **If there is a need to infuse money into the entity (beyond guaranteeing QFCs or otherwise buying/guaranteeing prepetition claims), the relevant government agency can participate by providing debtor-in-possession (DIP) financing, subject to the usual bankruptcy rules regarding priority.**

[39] Robert Eager, *supra* note 29.

Explanation While this makes possible a government" bailout," it would be subject to judicial oversight and bankruptcy code standards. As I note below (under "Alternative Proposals") it is very difficult to figure out a way to legally constrain the government from a "bailout" that it wants; my proposal at least has the judicial process involved, as well as the transparency of a judicial proceeding—both significant virtues. I also want to "hedge," in case there are some liquidity needs that would pass through the entity in bankruptcy that wouldn't fit into the ordinary DIP model (including priority).

Alternative Proposals H.R. 3310 proposes amending Bankruptcy Code § 364 to provide a new subsection (g) that provides "[n]othwithstanding any other provision of this section, the trustee may not, and the court may not, authorize the trustee to, obtain credit, if the source of that credit either directly or indirectly is the United States." (Interestingly, this provision is not limited to the proposed Chapter 14, nor is it limited to "non-bank financial institutions," which otherwise are the subject of H.R. 3310.) This provision seems designed to prevent "bailout" under the auspices of "bankruptcy." It is, however, both too broad and too narrow. It is too broad in that there may be cases in which financial stability can be enhanced by the government providing DIP funding, subject to the rules and processes of the Bankruptcy Code. Not all government-supplied DIP funding will necessarily function as a "bailout," in the sense of rescuing prepetition claimants (indeed, DIP funding, by its nature, does not itself go to prepetition claimants). It is too narrow in that the major way in which the government can "bail out" prepetition claimants is not affected by this provision. Whether through guarantees or purchases, the government is always able to "rescue" prepetition claimants, and then, by assignment or subrogation, assert those claims in the bankruptcy process. No bankruptcy court permission is needed to accomplish this, and a provision blocking the government's "trading in claims" would be very difficult, if not impossible, to draft without significant overbreadth concerns. Moreover—to use as an example—the Chrysler bankruptcy (to which this provision of H.R. 3310 would have applied)—the government provided TARP funding to Chrysler pre-bankruptcy and operating funds to the "new" Chrysler formed as a result of the § 363 sale. Neither of these two provisions of government funds would have been touched by H.R. 3310, since neither occurred under § 364—nor, indeed, within bankruptcy. Given this, I think it is preferable to not change the current bankruptcy provisions regarding DIP funding, but subject it to bankruptcy court oversight and control.

- **Funding for sums expended by the relevant government agency on guarantees, DIP financing, special masters (and their staff), etc., would be**

developed in a manner as it would for any sort of resolution authority system.

Explanation The obvious analogy is the fund created for the resolution of depository banks by the FDIC. I toyed with the idea of having some of the costs imposed on the bankrupt entity's creditors—to provide an incentive, for example, for better monitoring. But I also worried that if the government is able to "shift" the cost of what it is doing to creditors, it might be too willing to guarantee, provide funding, and the like. (I think of Chrysler here.) Thus, I conclude by thinking it best to leave this to whatever system ("taxes" on relevant firms, or whatever) might be considered for a non-bankruptcy resolution system. The goal is to have the creditors (and shareholders) of the failed financial institution be neither *advantaged* (through funds "rescuing" the financial institution because of systemic concerns that improve the creditors' positions) nor *disadvantaged* (through processes—think Chrysler—designed to reorder pre-existing priorities based on political considerations) by the government's concerns about systemic consequences. That should, ultimately, be the goal of any statutory changes and judicial oversight.