Understanding Failure: Examiners and the Bankruptcy Reorganization of Large Public Companies

by

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> "An examiner's legal status is unlike that of any other court-appointed officer which comes to mind."[1]
>
> "While we are examining into everything we sometimes find truth where we least expected it."[2]

INTRODUCTION

How do we learn from—and about—our mistakes?

When a business succeeds, it will be in a position to tell the world how and why it built a better mousetrap. Success has a thousand parents. Failure, however, is an orphan—for good reason. Business failures reflect mistakes of judgment, timing, execution, serious wrongdoing, or simple bad luck. Whatever the reason, few of us want to crow about our defeats. Even fewer would want to pay someone to do it for us. Yet, chapter 11 of the United

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[1] *In re* Baldwin United Corp., 46 B.R. 314, 316 (Bankr. S.D. Ohio 1985).

[2] MARCUS FABIUS QUINTILIAN, INSTITUTES OF ORATORY XII.8.10 (Lee Honeycutt ed., John Selby Watson trans., Iowa State University 2006) (1856), *available at* http://honeyl.public.iastate.edu/quintilian ("for, by searching into every particular, we sometimes discover truth where we least expected to find it").

States Bankruptcy Code, the principal legal mechanism for resolving business distress under U.S. law,[3] was predicated in part on creating a mechanism for doing just that, through the role of the "examiner."

Examiners are private individuals appointed by the United States Trustee at the direction of a bankruptcy court to investigate and report on alleged acts of pre-bankruptcy mal- or mis-feasance when a company seeks protection under chapter 11.[4] Congress created examiners to provide "special protection for the large cases having great public interest . . . to determine fraud or wrongdoing on the part of present management."[5] Examiners have played important, often controversial, roles in many of our most recent, high-profile bankruptcy cases, including *Enron,*[6] *Worldcom*,[7] *Refco*,[8] *Mirant,*[9] *New Century*,[10] *Lyondell Chemical,*[11] and *Lehman Brothers*.[12] Their investigations on occasion have cost millions of dollars[13] and resulted in major lawsuits or settlements.[14]

The central questions about examiners are, in a sense, existential: When will they be sought and appointed? Many read the Bankruptcy Code to mean that an examiner must be appointed if sought in a case with a "large" debtor. Bankruptcy Code § 1104(c)(2) provides that "on request of a party in interest . . . the court *shall* order the appointment of an examiner to con-

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[3]The current version of the Bankruptcy Code was originally enacted in 1978, (Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549), and has been amended several times, including in 2005, in ways that indirectly affect the appointment of examiners. Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA), Pub. L. No. 109-8, 119 Stat. 23 (codified as amended in scattered sections of 11, 18, 28 U.S.C.). These amendments are discussed in Part 1.5, *infra.*

[4]This paper analyzes examiners appointed under Bankruptcy Code § 1104(c)(2), not so-called "fee examiners" appointed to monitor the costs of professionals in certain large cases.

[5]124 CONG. REC. S17403-34 daily ed., Oct. 6, 1978 (quoted in COLLIER ON BANKRUPTCY, App. 14.4(f)(iii) (15th ed., Rev 2002)) [hereinafter COLLIER] (statement of Senator DeConcini).

[6]*In re* Enron Corp., No. 01-16034 (Bankr. S.D.N.Y. 2001).

[7]*In re* Worldcom, No. 02-13533 (Bankr. S.D.N.Y. 2002).

[8]*In re* Refco, Inc., No. 05-60006 (Bankr. S.D.N.Y 2005).

[9]*In re* Mirant Corp., No. 03-46591 (Bankr. N.D. Tex. 2003).

[10]*In re* New Century TRS Holdings, Inc., No. 07-10416 (Bankr. D. Del. 2007).

[11]Transcript of Hearing Before the Honorable Robert E. Gerber, at 35, *In re* Lyondell Chemical Co., No. 09-10023 (REG) (Oct. 26, 2009) (docket no. not available)(transcript on file with author) [hereinafter, *Lyondell Transcript*].

[12]*In re* Lehman Brothers Holdings, Inc., No. 08-13555 (Bankr. S.D.N.Y.). The 9-volume, 2000+page examiner's report in *Lehman Brothers* was released as this article was going to press. It was not possible to review that report for this discussion. *See* Report of Anton R. Valukas, Examiner, *In re* Lehman Brothers Holdings, Inc., No. 08-13555 (Bankr. S.D.N.Y. Mar. 11, 2010), *available at* http://lehmanreport.jenner.com (last visited Mar. 15, 2010).

[13]*See* Anthony Lin, *Enron Examiner Billed Estate for $100 Million: Batson Seeks End of Appointment for Inquiry*, N.Y.L.J., Dec. 5, 2003, at 1. *See infra* text at Part 2.2.5.

[14]The *Enron* examiner's fee application describes billions of dollars worth of claims discovered and notes subsequent litigation involving over a billion dollars of such claims. Examiners' Fee Application, at 4-5, 4 n. 5, *In re* Enron Corp., No. 01-16034, (Bankr. S.D.N.Y. Oct. 29, 2004) (No. 21686). Examiners' fees in the *Enron* case are discussed in note 214, *infra.* R

duct such an investigation of the debtor as is appropriate . . . if . . . the debtor's fixed, liquidated, unsecured debts, other than debts for goods, services, or taxes, or owing to an insider, exceed $5 million.[15] Senator DeConcini, addressing the legislation that became the Bankruptcy Code, said he believed that examiners would be appointed "automatically" in any large case in which a trustee was not appointed.[16] The only U.S. Court of Appeals to have considered the issue apparently agreed,[17] and other courts have followed suit.[18] It is thus not surprising that some commentators claim that examiners are "routinely" sought and appointed in large cases.[19]

Yet, judges are often reluctant to appoint an examiner if there is no apparent benefit to the estate or if a party requests one for transparently strategic reasons.[20] Judge Gerber recently railed against the seemingly mandatory lan-

[15] 11 U.S.C. § 1104(c)(2) (emphasis supplied) provides in full as follows:

> (c) If the court does not order the appointment of a trustee under this section, then at any time before the confirmation of a plan, on request of a party in interest or the U.S. Trustee, and after notice and a hearing, the court shall order the appointment of an examiner to conduct such an investigation of the debtor as is appropriate, including an investigation of any allegations of fraud, dishonesty, incompetence, misconduct, mismanagement or irregularity in the management of the affairs of the debtor of or by current or former management of the debtor, if—
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> (1) such appointment is in the interests of creditors, any equity security-holders, and other interests of the estate; or
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> (2) the debtor's fixed, liquidated, unsecured debts, other than debts for goods, services or taxes, or owing to an insider, exceed $5 million.

[16] *See* S. 17404 (daily ed. Oct. 6, 1978) ("There will automatically be appointed an examiner in [large cases], but not a trustee . . . . I am convinced that debtor and creditor interests, as well as the public interest, will be preserved and enhanced by these provisions") (statement of Sen. DeConcini).

[17] *In re* Revco D.S., Inc., 898 F.2d 498, 501 (6th Cir. 1990); ("Section 1104(b)(1), which governs the appointment of an examiner when the total unsecured debt is less than $5 million, follows the language of § 1104(a) [the appointment of a trustee]; in both cases the appointment is left to the bankruptcy court's discretion. The contrast with § 1104(b)(2) could not be more striking. When the total 'fixed, liquidated, unsecured' debt is greater than $5 million, the statute requires the court to appoint an examiner.").

[18] *See, e.g., In re* Loral Space & Commc'ns, Ltd., 2004 WL 2979785 (S.D.N.Y., Dec. 23, 2004) (holding appointment mandatory) *rev'g* 313 B.R. 577 (Bankr. S.D.N.Y. 2004); *In re* UAL Corp., 307 B.R. 80 (Bankr. N.D. Ill. 2004) (same); *In re* Schepps Food Stores, Inc., 148 B.R. 27 (S.D. Tex. 1992) (same); *In re* Mechem Fin. of Ohio, Inc., 92 B.R. 760 (Bankr. N.D. Ohio 1988) (same); *In re* The Bible Speaks, 74 B.R. 511 (Bankr. D. Mass. 1987) (same); *In re* 1243 20th St., Inc., 6 B.R. 683 (Bankr. D.D.C. 1980) (same); *In re* Lenihan, 4 B.R. 209 (Bankr. D.R.I. 1980) (same).

[19] *See, e.g.*, A. Mechele Dickerson, *Privatizing Ethics in Corporate Reorganizations*, 93 MINN. L. REV. 875, 903 (2009) ("Whether or not examiners *must* be appointed in large business Chapter 11 reorganizations, they routinely *are* appointed in these cases . . . ."); Stanley A. Kaplan, *The Role of Examiner: Some Observations*, 4 BANKR. DEV. J. 439, 439 (1987) (claiming that examiners were "being appointed in most major reorganizations and [that] the role of the examiner [became] a rather significant one."). *See also* Elizabeth Warren & Jay L. Westbrook, *Examining the Examiners*, 24 AM. BANKR. INST. J. 34 (May 2005) ("Reading recent cases about examiners, we were having trouble finding a standard by which to understand the analysis, so we cheated and looked at the relevant provisions of the statute. We came away thinking that the courts and the academics may have lost track of just what Congress said.").

[20] *See, e.g.*, *In re* Bradlees Stores, Inc., 209 B.R. 36 (Bankr. S.D.N.Y. 1997) (waiver of right to appoint an examiner by delay in seeking appointment); *In re* Am. Home Mortgage Holdings, Inc., No. 07-11047 (CSS)

guage of the statute. "[M]andatory appointment [of examiners] is terrible bankruptcy policy," he noted in the *Lyondell Chemical* case, "and the Code should be amended, forthwith, to delete § 1104(c)(2), and to give bankruptcy judges (subject to appellate review, of course) the discretion to determine when an examiner is necessary and appropriate, and whether a request for an examiner is merely a litigation or negotiating ploy."[21] Many would agree with the view that one should not be able to "cry 'examiner' in a crowded case, [and] get one."[22]

Although there is a wealth of empirical data on business bankruptcy,[23] there has been no attempt to understand the pattern in the appointment of examiners. This paper helps to fill that gap. A review of dockets from 576 of the largest chapter 11 cases commenced between 1991 and 2007 indicates that examiners were requested in only eighty-seven cases, or about 15% of the sample.[24] The motions were granted in only thirty-nine cases, less than half of cases where sought, and about 6.7% percent of *all* cases in the sample.[25] The takeaway point is clear: Examiners are neither "routinely" sought nor "automatically" appointed in large cases.

(Bankr. D. Del., Oct. 31, 2007) (declining to appoint examiner on grounds that, even if the statutory threshold is satisfied, "there has to be an investigation to perform that's appropriate") (transcript at 76) [hereinafter *American Home Transcript*]; *In re* S.A. Telecomms., Inc., Nos. 97-2395 (PJW) through 97-2401 (PJW) (Bankr. D. Del., Mar. 27, 1998) ("I'm going to point out that this Court has for years consistently viewed [§ 1104(c)(2)] as not being a mandatory provision . . . . My view doesn't turn on the word 'shall' and I've ruled a number of times to this effect, Judge Balick has, and I think I'm not going to change this Court's view of that section.").

[21] *See Lyondell Transcript, supra* note 11, at 35. R

[22] *See American Home Transcript, supra* note 20, at 76. R

[23] Much of this work comes from Professors Lynn LoPucki, Elizabeth Warren and Jay Westbrook. *See, e.g.*, LYNN M. LOPUCKI, COURTING FAILURE: HOW COMPETITION FOR BIG CASES IS CORRUPTING THE BANKRUPTCY COURTS (Michigan 2005) [hereinafter LOPUCKI, FAILURE]; Lynn M. LoPucki & William C. Whitford, *Corporate Governance in the Bankruptcy Reorganization of Large, Publicly Held Corporations*, 141 U. PA. L. REV. 669 (1993); Lynn M. LoPucki, & Joseph W. Doherty, *Bankruptcy Fire Sales*, 106 MICH. L. REV. 1 (2007); Elizabeth Warren & Jay Lawrence Westbrook, *Financial Characteristics of Businesses in Bankruptcy*, 73 AM. BANKR. L.J. 499 (1999); Elizabeth Warren & Jay Lawrence Westbrook, *Contracting Out of Bankruptcy: An Empirical Intervention*, 118 HARV. L. REV. 1197, 1237-38 (2005); Elizabeth Warren & Jay Lawrence Westbrook, *The Success of Chapter 11: A Challenge to the Critics*, 107 MICH. L. REV. 603 (2009). Other recent contributions in this vein include Douglas G. Baird & Edward R. Morrison, *Serial Entrepreneurs and Small Business Bankruptcies*, 105 COLUM. L. REV. 2310 (2005); Michelle M. Harner, *Trends in Distressed Debt Investing: An Empirical Study of Investors' Objectives*, 16 AM. BANKR. INST. L. REV. 69 (2008); Stephen J. Lubben, *Corporate Reorganization & Professional Fees*, 82 AM. BANKR. L.J. 77 (2008).

[24] The data build on a sample of 576 "large" chapter 11 cases commenced between 1991 and 2007 drawn from Professor Lynn LoPucki's Bankruptcy Research Database of large chapter 11 cases (the "BRD"). LoPucki has created a database of all large chapter 11 bankruptcy cases commenced since 1980. *See* Bankruptcy Research Database, http://www.webbrd.com (last visited Sept. 16, 2009). This paper draws on data from the BRD as of June 2007. Although the BRD presents data on many attributes of these cases, it contains no data on the use of examiners.

[25] As discussed further below, it appears examiners were appointed sua sponte, or at least without any written motion, in three cases. *See In re* Baldwin Builders, No. 95-13057 (Bankr. S.D. Cal. 1995); *In re* El

The data, in turn, beg important questions: If they are not mandatory (if sought), when will they be sought and appointed? What factors—other than the statute—matter? If, instead, they are viewed as mandatory, why are they so rare? Why do bankruptcy courts—guided (perhaps burdened) by a legacy of strict textualism[26]—resist Congress' (fairly clear) language and expressed intent? In any case, once appointed, what do they actually do? What value, if any, do they bring to the process of reorganizing troubled businesses, and how do we measure that value?

This paper presents hand-collected, docket-level and interview data that help to answer these questions. Major findings include the following:

- *Size matters.* Cases in which examiners are sought are huge. The average case in which an examiner was sought was almost twice as large as the sample measured by median asset values and more than four times larger measured by mean asset values. Holding other things equal, a request for an examiner was three times more likely in a case with a debtor having at least $100 million in net assets. Cases in which examiners were appointed had mean liabilities twice the size of cases where the motions were not granted.
- *Conflict matters.* Cases in which examiners were sought or appointed were much more likely to be contentious, as measured by docket size and requests for chapter 11 trustees, than were cases without. Holding other things equal, a request for a chapter 11 trustee in a large case increases the odds of an examiner request by a factor of five.
- *Venue matters.* Examiners are much more likely to be sought—although not necessarily appointed—in the two districts that tend to have the largest cases, Delaware and the Southern District of New York (SDNY). Together, Delaware and the SDNY had forty-six (52% of) requests for an examiner, but actually appointed an examiner in only

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Paso Refinery, LP, No. 94-30051 (Bankr. W.D. Tex. 1992); *In re* Bonneville Pac. Corp., No. 91-27701 (Bankr. D. Utah 1991).

[26] *See, e.g.*, Bruce A. Markell, *Conspiracy, Literalism and Ennui at the Supreme Court*, 41 FED. B. NEWS & J. 174, 177 (1994) (observing that strict textualism "concentrate[s] more on a policy of good grammar than on good bankruptcy policy"); Charles Jordan Tabb & Robert M. Lawless, *Of Commas, Gerunds and Conjunctions: The Bankruptcy Jurisprudence of the Rehnquist Court*, 42 SYRACUSE L. REV. 823 (1991).

The Supreme Court's experiments with strict construction in bankruptcy include Fla. Dep't of Revenue v. Piccadilly Cafeterias, Inc., 128 S. Ct. 2326, 2338-39 (2008) (textual analysis of Bankruptcy Code § 1146); Patterson v. Shumate, 504 U.S. 753, 757-58 (1992) (using "plain language" of § 541(c)(2) of Bankruptcy Code to determine if ERISA-qualified pension plan constitutes restriction on transfers); Union Bank v. Wolas, 502 U.S. 151, 155-56 (1991) (using legislative history to support "literal reading" of Bankruptcy Code); Toibb v. Radloff, 501 U.S. 157, 160 (1991) (using "plain language" of Bankruptcy Code to decide whether non-business debtor may reorganize under Chapter 11); United States v. Ron Pair Enters., Inc., 489 U.S. 235, 242 (1990) (plain language should be used when reading statutes).

seventeen cases (about 43%, n=39).[27] By contrast, examiners were appointed in twenty-two cases (about 57% of appointments) when requested in other districts.

- *Fraud matters—somewhat.* Although requests for an examiner correlated with allegations of pre-bankruptcy fraud—the paradigm grounds for an examiner—they were nevertheless rare even when a bankruptcy was precipitated by that form of wrongdoing: Of the thirty-one cases in the sample that allegedly involved fraud, examiners were sought in only nine and, of those, were appointed in only five.
- *Strategy matters—somewhat.* There is evidence that examiners will sometimes be sought for strategic, not information-seeking, reasons. Requests to appoint an examiner were withdrawn in fourteen cases (about 17% of requests in the sample) and rendered moot by subsequent events (e.g., plan confirmation) in sixteen cases (about 20% of requests). Judges and system participants interviewed for this paper indicated that they believed that, in many cases, the arguably "mandatory" language of the Bankruptcy Code produces gamesmanship, not enlightenment.
- *Investors do not matter much.* Notwithstanding a purported goal of protecting the "investing public," individual investors made only eighteen requests for examiners. Far more likely to request an examiner (thirty-two cases) were individual creditors whose claims did not arise from investment securities (such as bonds) or fraud, but who apparently held claims for unpaid goods or services.

This paper proceeds as follows: Part 1 describes the doctrinal and historic background of examiners, emphasizing the role that investigation has played in reorganization policy and process. Part 2 describes the data, methodology and cases examined. Parts 3 and 4 use the data to explain the factors that correlate to examiner appointments and to discuss what they do. Part 5 considers why they have been so rare. Part 6 concludes with observations about the implications of the data and recommendations for further action.

1. BACKGROUND—HISTORY AND DOCTRINE

Although bankruptcy examiners have enjoyed a certain amount of recent attention—due in large part to their prominent roles in the *Enron*, *Worldcom*, *Refco,* and *Lehman Brothers* cases—they and the questions they present are not new to the system. They, and the investigative function they perform, have been bound up in important policy debates about the goals and role of reorganization under U.S. law for many years. These policy debates have

[27]For those not trained in statistics, "n" refers to the number of cases observed for the stated proposition.

resulted in various bankruptcy laws which, in chronological terms, can be understood as those in force before 1938, and those enacted from and after 1938, when the role of the examiner was first formally made part of the corporate bankruptcy process.

1.1 PRE-1938

Beginning in the late 19th century, Congress sought to create a permanent mechanism to understand and learn from corporate failure. In the 1880s, John Lowell, a federal judge from Massachusetts, was recruited by creditor groups to develop bankruptcy legislation based on the English model, which tended to give creditors significant control over the bankruptcy process.[28] In 1882, a Lowell bill was introduced, under which federal judges overseeing bankruptcy cases would appoint bankruptcy supervisors.[29] These supervisors would, among other things, examine the administration of bankruptcy proceedings, advise referees and trustees on administrative matters, and report to the courts any misconduct on the part of trustees, filling the role of independent observer.[30] They would have functioned much as examiners were expected to function under current law. Although Lowell's bill passed the Senate in 1884, it was supplanted by Representative Torrey's bill, enacted as the Bankruptcy Act of 1898.[31] While the Torrey bill borrowed heavily from Lowell's legislation, bankruptcy supervisors were not part of the package.

The Bankruptcy Act of 1898 was problematic for many reasons. Perhaps the principal problem was that failure was really addressed by two distinct systems, not one. On the one hand, there was the formal bankruptcy law in place at the time, the Bankruptcy Act of 1898, which governed individual bankruptcies and generally goaded business debtors toward liquidation rather than reorganization. Because a case under the Bankruptcy Act resulted in the appointment of a trustee, it held little appeal for managers of the nation's largest corporations, in particular the railroads, almost all of which encountered major financial distress at one time or another. On the other hand, there was a second system that large corporate debtors (e.g., railroads) used, the federal equity receivership.[32] This was a process wholly outside the

[28]*See* DAVID A. SKEEL, JR., DEBT'S DOMINION: A HISTORY OF BANKRUPTCY LAW IN AMERICA 36 (Princeton Univ. Press 2001).

[29]S. DOC. NO. 1382, 47th Cong. (2d Sess. 1882).

[30]*Id.*

[31]Ch. 541, 30 Stat. 544 (1898), *repealed by* Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549. *See also* David A. Skeel, Jr., *The Genius of the 1898 Bankruptcy Act*, 15 BANKR. DEV. J. 321, 329 (Spring 1999).

[32]This system is described in greater detail in Jonathan C. Lipson, *The Expressive Function of Directors' Duties to Creditors*, 12 STAN. J.L. BUS. & FIN. 224, 231-45 (2007) and Jonathan C. Lipson, *The Shadow Bankruptcy System,* 89 B.U. L. REV. 1609 (2009). The seminal texts describing the practice were

scope of the bankruptcy law at the time,[33] and was largely a creation of the managers, lawyers and bankers involved with the company.

Neither system created incentives or mechanisms to learn from failure. Trustees under the Bankruptcy Act might have investigated the debtor's assets, but only because their compensation was tied to the hunt; trustees ate what they killed. The equity receivership might require a solicitation of votes from security holders, which in turn might require some disclosures about the proposed reorganization plan, but the so-called "protective committees" that often pulled the strings had no reason to investigate or explain how and why the companies whose investors they "protected" had failed in the first place.[34]

The investigative function in bankruptcy was revived during the Depression, although examiners were not a part of it. The 1931 Thacher Report[35] found existing procedures for investigation lacking, stating that "[t]he wholesale discharge of bankrupts, practically without inquiry or opposition, [was] seriously detrimental to the public interest because it encourages dishonest and reckless disregard of just obligations and thus destroys the integrity of the individual."[36] The Thacher Report recommended that Congress create a body of officials to examine debtors in every case, assisting trustees and reporting crimes to the United States Attorney.[37] Bankruptcy trustees, who were permitted to have an interest in the proceedings, were not to complete the tasks assigned to examining officials.[38] Although Congress amended the 1898 Bankruptcy Act in 1934 to include § 77B, reforming corporate reorganization, it still failed to provide for the appointment of examiners.[39]

Arthur H. Dean, *Corporate Reorganization*, 26 CORNELL L. Q. 537, 538-39 (1941) and Paul D. Cravath, *The Reorganization of Corporations; Bondholders' and Stockholders' Protective Committees; Reorganization Committees; and the Voluntary Recapitalization of Corporations*, *in* SOME LEGAL PHASES OF CORPORATE FINANCING, REORGANIZATION AND REGULATION 153 (MacMillan Co. 1917).

[33]Certain aspects of the equity receivership were ultimately codified in what came to be known as § 77, *see* Act of Mar. 3, 1933, ch. 204 § 77, 47 Stat. 1474 (1933) (codified prior to repeal at 11 U.S.C. § 205 (1976)) (pertaining to railroad reorganizations), and § 77B, *see* Act of June 7, 1934, ch. 424 § 77B, 48 Stat. 912 (1934) (codified prior to repeal in scattered sections of 11 U.S.C.) (pertaining to other corporations).

[34]*See* Lipson, *Shadow Bankruptcy*, *supra* note 32. R

[35]STRENGTHENING OF PROCEDURE IN THE JUDICIAL SYSTEM: THE REPORT OF THE ATTORNEY GENERAL ON BANKRUPTCY LAW AND PRACTICE, S. DOC. NO. 72-65 (1932).

[36]*Id.* at 13.

[37]*Id.* at 93.

[38]*Id.* at 95-96.

[39]Act of June 7, 1934, ch. 424, 48 Stat. 911, 912, 11 U.S.C. § 207 (repealed).

The lack of specific legislation giving courts the power to appoint examiners, however, did not prevent them from doing so, in their equitable discretion. In *In re Utilities Power & Light Corp.*, for example, the Seventh Circuit observed that "[i]t has long been the rule that courts of equity administering estates may call to their help commissioners, auditors, accountants, appraisers, examiners or masters." Clark v. Utilities. Power & Light Corp. (*In re* Utils. Power & Light Corp.), 90 F.2d 798, 800 (7th Cir. 1937). The power "grow[s] out of judicial necessity in order to achieve equity, and its exercise is based upon a finding, under

The strongest proponent of the inherent value of understanding failure was William O. Douglas, perhaps the most prominent bankruptcy scholar of his time.[40] His 1934 report on the reorganization system laid the groundwork for wholesale reforms, including the introduction of mandatory investigations in large cases.[41] This report, which was ordered in connection with adoption of the Securities Exchange Act of 1934,[42] was heavily influential in laying the foundation for the current reorganization system, including much of its informational architecture.

For Douglas, investigation (and disclosure) played two different, but related, roles. Information-forcing through *ex ante* disclosure and *ex post* investigation would promote fair and efficient capital markets because investors would have the information they needed to make intelligent investment decisions. It would also deter misconduct, shaming those who might abuse positions of trust into conforming their conduct to acceptable social standards.[43] Douglas' goals were as much informational as they were procedural: he wanted to create a system that would oust the "reorganizers," the managers, bankers and advisors who, he believed, manipulated the restructuring process for their own benefit to the detriment of the investing public. Thus, he believed that in all large business cases, a trustee with investigative powers should be appointed to displace management. Although investigation of the reasons for the debtor's failure would not be the trustee's sole job, it was central to Douglas' vision of the reorganization process.

1.2 The Chandler Act of 1938

Douglas's approach to business reorganization was, in many respects, re-

rules of legal discretion, that, without aid to the court, the issues cannot be dealt with intelligently, efficiently or promptly." *Id.* (*citing* Burnrite Coal Co. v. Riggs, 247 U.S. 208 (1927); Thiede v. Utah, 159 U.S. 510 (1895); Fenno v. Primrose, 119 F. 801 (1st Cir. 1903); Destructor Co. v. City of Atlanta, 232 F. 746 (N.D. Ga. 1916)).

[40]*See* David A. Skeel, Jr., *Vern Countryman and the Paths of Progressive (and Populist) Bankruptcy Scholarship*, 113 Harv. L. Rev. 1075, 1079 (2000) ("It is no exaggeration to say that, during the decade from roughly 1928 to 1938, Douglas figured prominently in every significant development affecting bankruptcy law and bankruptcy theory."). The articles that emerged from Douglas's work include William Clark, William O. Douglas & Dorothy S. Thomas, *The Business Failures Project – A Problem in Methodology*, 39 Yale L.J. 1013 (1930); William O. Douglas & Dorothy S. Thomas, *The Business Failures Project – II. An Analysis of Methods of Investigation*, 40 Yale L.J. 1034 (1931); William O. Douglas & J. Howard Marshall, *A Factual Study of Bankruptcy Administration and Some Suggestions*, 32 Colum. L. Rev. 25 (1932); William O. Douglas, *Some Functional Aspects of Bankruptcy*, 41 Yale L.J. 329 (1932); William O. Douglas, *Wage Earner Bankruptcies – State vs. Federal Control*, 42 Yale L.J. 591 (1933).

[41]Sec. and Exch. Comm'n, Report on the Study and Investigation of the Work, Activities, Personnel and Functions of Protective and Reorganization Committees (1936-1940) [hereinafter Douglas Report].

[42]*See* Securities Exchange Act of 1934, Pub. L. No. 73-291, §§ 4, 211, 48 Stat. 881, 885, 909 (1934) (codified as amended at 11 U.S.C. §§ 78a-78nn (2006)).

[43]*See, e.g.*, Douglas Report, *supra* note 41, at 693-94 (finding secrecy "inimical to the interests of investors and creditors as a whole"). R

flected in the 1938 Chandler Act, which completely revamped the 1898 Bankruptcy Act.[44] The Chandler Act made investigation a high priority for cases involving debtors with debts in excess of $250,000.[45] In these cases, governed by Chapter X, a trustee was to be appointed, whose duties prominently included an investigation and report to the judge.[46] If a case under Chapter X involved debts less than $250,000, management of the debtor may have been permitted to continue to operate the debtor, but the Chandler Act permitted a court to appoint a disinterested examiner to perform the role of the trustee.[47] Examiners possessed the full authority of a trustee short of

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[44]*See* Chandler Act § 156, 52 Stat. at 888, 11 U.S.C. § 567 (1938) (repealed). *See also* David S. Kennedy & R. Spencer Clift, III, *An Historical Analysis of Insolvency Laws and Their Impact on the Role, Power, and Jurisdiction of Today's United States Bankruptcy Court and its Judicial Officers*, 9 J. BANKR. L. & PRAC. 165, 176 (2000); Eric A. Posner, *The Political Economy of the Bankruptcy Reform Act of 1978*, 96 MICH. L. REV. 47, 64 (1997).

[45]Chandler Act § 156, 52 Stat. at 888, 11 U.S.C. § 567 (1938) (repealed):

> Upon the approval of a petition, the judge shall, if the indebtedness of a debtor, liquidated as to amount and not contingent as to liability, is $250,000 or over, appoint one or more trustees. Any trustee appointed under this chapter shall be disinterested and shall have the qualifications prescribed in section 45 of this Act, except that the trustee need not reside or have his office within the district. If such indebtedness is less than $250,000, the judge may appoint one or more such trustees or he may continue the debtor in possession. In any case where a trustee is appointed the judge may, for the purposes specified in section 189 of this Act, appoint as an additional trustee a person who is a director, officer, or employee of the debtor.

[46]Chandler Act § 167, 52 Stat. at 890, 11 U.S.C. § 567 (1938) (repealed):

> The trustee upon his appointment and qualification
> (1) shall, if the judge shall so direct, forthwith investigate the acts, conduct, property, liabilities, and financial condition of the debtor, the operation of its business and the desirability of the continuance thereof, and any other matter relevant to the proceeding or to the formulation of a plan, and report thereon to the judge;
> (2) may, if the judge shall so direct, examine the directors and officers of the debtor and any other witnesses concerning the foregoing matters or any of them;
> (3) shall report to the judge any facts ascertained by him pertaining to fraud, misconduct, mismanagement and irregularities, and to any causes of action available to the estate;
> (4) may, subject to the approval of the judge, employ such person or persons as the judge may deem necessary for the purpose of assisting the trustee in performing the duties imposed upon him under this chapter;
> (5) shall, at the earliest date practicable, prepare and submit a brief statement of his investigation of the property, liabilities, and financial condition of the debtor, the operation of its business and the desirability of the continuance thereof, in such form and manner as the judge may direct, to the creditors, stockholders, indenture trustees, the Securities and Exchange Commission, and such other persons as the judge may designate; and
> (6) shall give notice to the creditors and stockholders that they may submit to him suggestions for the formulation of a plan, or proposals in the form of plans, within the time therein named.

[47]Chandler Act § 168, 52 Stat. at 890, 11 U.S.C. § 567 (1938) (repealed):

soliciting interested parties when formulating a plan of reorganization.[48]

In certain respects, an examiner in these large cases would have been redundant because the investing public was also protected by the Securities and Exchange Commission, which had a much more prominent role in large reorganizations than it has under current law. Under Chapter X of the Bankruptcy Act, the SEC had standing to act as a party in interest during the entire bankruptcy proceeding.[49] Any plan of reorganization for a debtor with more than $3 million in debt had to be submitted to the SEC for comment prior to confirmation.[50] The SEC vigorously fulfilled its watchdog role, participating in meetings, challenging the appointment of trustees and trustees' administrations, opposing plans of reorganization, and criticizing compensation agreements.[51] The SEC was to investigate past wrongdoing and to protect the investing public during the reorganization process.[52]

Although Chapter X held the promise of creating a mechanism for learning from failure, it was flawed: like the Bankruptcy Act of 1898, there remained two systems. In this case, the second system was not equity receiverships but Chapter XI.[53] Chapter XI permitted management of a debtor to remain in possession without investigation by a trustee or examiner.[54] Chapter XI was designed to provide relief to small, privately held companies, but its terms were not so limited and large public companies sought to file under it.[55] The SEC was originally able to isolate this defect by convincing courts to foreclose public companies from Chapter XI relief,[56] but the 1956 Supreme Court decision in *General Stores Corp. v. Shlensky* eviscerated the public/private distinction, permitting even publicly held cor-

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> If a debtor is continued in possession, the judge may at any time appoint a disinterested person as examiner to prepare and file a plan and to perform the duties imposed upon a trustee under paragraphs (1) to (5), inclusive, of section 167 of this Act, or to perform any of such duties.

[48]*Id.*

[49]*Id.*

[50]Chandler Act § 172, 52 Stat. at 890-91 (1938) (repealed).

[51]*See* Posner, *supra* note 44, at 65, 110 (1997) ("In Chapter X the SEC challenged trustees who had connections with management, monitored their administration of the estate, and opposed any procedures and arrangements that did not meet its standard of fairness."). R

[52]*See* Warren & Westbrook, *supra* note 19, at 34. R

[53]Chandler Act ch. 11, 52 Stat. 840, 905-16 (1938) (repealed).

[54]SEC v. U.S. Realty & Improvement Co., 310 U.S. 434, 450-51 (1940); Clifford J. White, III & Walter W. Theus, Jr., *Chapter 11 Trustees and Examiners After BAPCPA*, 80 AM. BANKR. L.J. 289, 292 (2006).

[55]Leonard L. Gumport, *The Bankruptcy Examiner*, 20 CAL. BANKR. J. 71, 83 (1992); David A. Skeel, *An Evolutionary Theory of Corporate Law and Corporate Bankruptcy*, 51 VAND. L. REV. 1325, 1374 (1998).

[56]*See* Skeel, *supra* note 55, at 1374; *see, e.g.,* U.S. Realty, 310 U.S. at 457-58 (1940) (permitting a court to compel filing under Chapter X to "safeguard public and private interests").

porations to file for relief under Chapter XI.[57] By the early 1970's, Chapter XI had become the "dominant reorganization vehicle" for companies of all sizes.[58]

1.3 The Modern Examiner—Compromise and the Bankruptcy Code of 1978

In response to growing dissatisfaction with, and unrest within, the bankruptcy system under the Chandler Act, Congress established the Commission on the Bankruptcy Laws of the United States in 1970 to identify and assess problem areas.[59] After two years of study, the Commission filed its recommendations for changes to "reflect and adequately meet the demands of present technical, financial, and commercial activities."[60] To effectuate these recommendations, the Commission submitted statutory amendments, culminating in the proposed Bankruptcy Act of 1973.[61]

While the Commission acknowledged the value of an independent trustee, it found the mandatory ouster of management and the trustee's assumption of authority (as under the unpopular Chapter X) to be unduly harsh.[62] The Commission instead suggested the discretionary appointment of independent trustees.[63] For cases where indebtedness exceeded $1 million, a trustee would presumptively be appointed unless a court found the protection unnecessary or disproportionate to the costs.[64] Were an independent trustee not appointed, any party in interest could ask the court to appoint an independent person to investigate—an examiner.[65] The Commission's bill was introduced in the House, but was replaced by House Bill 8200 in 1977.[66]

The original Senate version of the legislation that ultimately would become the Bankruptcy Code, S. 2266, addressed the concerns of the Securities and Exchange Commission by requiring in § 1104(a) the appointment of a trustee in any chapter 11 case involving a public company, defined in

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[57]Gen. Stores Corp. v. Shlensky, 350 U.S. 462, 466 (1956) ("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 we can see 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.").

[58]Report of the Commission on the Bankruptcy Laws of the United States, Pt. I, H.R. Doc. No. 93-137 (1973).

[59]Pub. L. No. 91-354, 84 Stat. 468 (July 24, 1970).

[60]1973 Commission Report , *supra* note 58 (citing introductory letter). R

[61]*Id.*

[62]1973 Commission Report, *supra* note 58, at 237, 248; Barry L. Zaretsky, *Trustees and Examiners in Chapter 11*, 44 S.C. L. Rev. 907, 921 (1993). R

[63]Zaretsky, *supra* note 62. R

[64]*Id.*

[65]*Id.*

[66]H.R. 8200, 95th Cong. (1st Sess. 1977). *See also* S. Rep. No. 95-989, 95th Cong., at 114-15 (2d Sess. 1978), *reprinted in* Collier, App. Pt. 4(e)(i), at App. Pt. 4-2071; *In re Lenihan*, 4 B.R. 209, 211 (Bankr. D. R.I. 1980).

§ 1101(3) as a debtor with outstanding liabilities of $5,000,000 or more, excluding liabilities for goods, services, or taxes, and not less than 1,000 security holders.[67] The House version, H.R. 8200, contained no provision that a trustee be appointed in a reorganization proceeding based on the liabilities of a public corporation, but rather required the court to consider the appointment of a trustee on a case-by-case basis.[68]

Although the House considered appointment of a trustee crucial (to protect both the general public and the creditors of particular companies) the standards for appointing a trustee were elusive. "The development of a standard for the appointment of a trustee or examiner in a chapter 11 reorganization case has been one of the more difficult issues in the bill," the House report explained.[69] "The difficulty arises in part because there is no comparable provision in current law to rely on. Instead . . . [C]hapter X requires the appointment of a trustee in every case; [C]hapter XI never permits appointment of a trustee."[70]

The House report hoped for the best of both worlds: "The twin goals of the standard for the appointment of a trustee should be protection of the public interest and the interests of creditors, as contemplated in current [C]hapter X, and facilitation of a reorganization that will benefit both the creditors and the debtors, as contemplated in current [C]hapter XI."[71] Although this passage mentioned only trustees—not examiners—the House drafters likely viewed them interchangeably. The same report shortly thereafter observed that "[t]he standards for determining whether to order the appointment of an examiner are the same as those for appointment of a trustee: the protection must be needed and the cost not disproportionately high."[72]

Eventually, the House and Senate reached a compromise in the final version, H.R. 8200, whereby the Senate's reference to a mandatory trustee in public company cases was eliminated and replaced with a mandatory exam-

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[67]Section 1101(3) in S. 2266 originally provided as follows: "'public company' shall mean a debtor who, within twelve months prior to filing a petition for relief under this chapter, had outstanding liabilities of $5,000,000 or more, exclusive of liabilities for goods, services, or taxes and not less than 1,000 security holders." *See* S. 2266, 95th Cong. § 1101(3) (2d Sess.1978), *reprinted in* COLLIER, App. Pt. 4(e), at App. Pt. 4-1849.

Section 1104(a) in S. 2266 originally provided as follows: "In the case of a public company, the court, within ten days after the entry of an order for relief under this chapter, shall appoint a disinterested trustee." S. 2266, 95th Cong. § 1104(a), (2d Sess. 1978), *reprinted in* COLLIER, App. Pt. 4(e), at App. Pt. 4-1850.

[68]*See* H.R. REP. NO. 95-595, 95th Cong., at 402 (1st Sess. 1977), *reprinted in* COLLIER, App. Pt. 4(d)(i), at App. Pt. 4-1550; *see also Lenihan*, 4 B.R. at 211.

[69]H.R. REP. NO. 95-595, at 232.

[70]*Id.*

[71]*Id.*

[72]*Id.* at 234.

iner (if requested by a party in interest) in § 1104(b)(2) (now § 1104(c)(2)).[73] An inference from this decision is that bankruptcy courts should have no discretion, and engage in no cost-benefit analysis, when asked to appoint an examiner. That, of course, has become conflicted territory in practice. Nevertheless, as the final remnant of the "public company" exception from S. 2266, § 1104(c)(2) is evidence, at least to some, that the examiner exists to protect constituents in larger cases by assuring that third party investigation is available if a party in interest desires such intervention.[74]

1.4 Experience Under the Bankruptcy Code

As the product of compromise, it is not surprising that courts have struggled to understand whether Congress really meant that examiners should be appointed if requested in any reasonably large case, regardless of cost or need. Despite the seemingly compulsory language of § 1104(c), judicial responses to motions for the appointment of an examiner have been divided.[75] Some courts treat appointment as mandatory when requested in a case with a large debtor.[76] Others view the appointment of an examiner to be discretionary, regardless of debtor size, especially where a judge has strong concerns about whether the appointment would benefit the estate.[77]

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[73]*See* 124 Cong. Rec. H11, 102 (daily ed. Sept. 28, 1978) (statement of Rep. Edwards), *reprinted in* Collier, App. Pt. 4(f)(i), at App. Pt. 4-2465; 124 Cong. Rec. S 17,419 (daily ed. Oct. 6, 1978) (statement of Sen. DeConcini), *reprinted in* Collier, App. Pt. 4(f)(iii), at App. Pt. 4-2579; *Lenihan*, 4 B.R. at 211. In the final version of the bill, the public company requirement, i.e., that the debtor have not less than 1,000 security holders, was also eliminated with respect to the mandatory appointment of an examiner, thus making such appointments applicable to all large debtors without regard to whether the debtor is a public company, so long as the unsecured debt limit is exceeded. *See* Lawrence K. Snider, *The Examiner in the Reorganization Process: A Need to Modify*, 45 Bus. Law. 35, 44 (1989-1990). One attorney interviewed for this project who claimed familiarity with the negotiations over the bill observed that the creation of the examiner was a "sop to the SEC." Email from L-3 to author, dated Nov. 16, 2009.

[74]Zaretsky, *supra* note 62, at 925-26 ("This was the last vestige of the Senate's insistence on an independent third party in public company cases. . . . It sought to protect constituents in larger cases by making available an independent third party when a party in interest felt a need for independent input."). R

[75]*See id.*, at 938 ("Although some courts have given effect to the mandatory language of [§ 1104(c)], other courts have refused to follow the command and have been unwilling to authorize the appointment of an examiner without a showing of need, even when the request is made by a party in interest in a case that meets the financial standard of [§ 1104(c)].").

[76]*In re* Revco D.S., Inc., 898 F.2d 498 (6th Cir. 1990); *In re* Schepps Food Stores, Inc., 148 B.R. 27, 30 (S.D. Tex. 1992); *In re* UAL Corp., 307 B.R. 80 (Bankr. N.D. Ill. 2004); *In re* Big Rivers Elec. Corp., 213 B.R. 962, 965-966 (Bankr. W.D. Ky. 1997); *In re* Mechem Fin. of Ohio, Inc., 92 B.R. 760, 761 (Bankr. N.D. Ohio 1988); *In re* The Bible Speaks, 74 B.R. 511, 514 (Bankr. D. Mass. 1987); *In re* GHR Cos., Inc., 43 B.R. 165, 168 (Bankr. D. Mass. 1984), *aff'd*, 792 F.2d 476 (5th Cir. 1986) (venue transferred from District of Massachusetts to Southern District of Texas after motion for examiner denied).*In re* Tyler, 18 B.R. 574, 578-579 (Bankr. S.D. Fla. 1982); *In re* 1243 20th Street, Inc., 6 B.R. 683, 685 n.3 (Bankr. D.D.C. 1980); *Lenihan*, 4 B.R. at 211. Some courts appear to believe that they have the power to appoint an examiner without a motion. *See, e.g.*, *In re* First Am. Healthcare of Ga., 208 B.R. 992, 994-995 (Bankr. S.D. Ga. 1996).

[77]*See In re* Bradlees Stores, Inc., 209 B.R. 36 (Bankr. S.D.N.Y. 1997) (finding waiver of right to appoint

In *In re GHR Cos.*,[78] for example, the United States Trustee and certain creditors moved for the appointment of an examiner.[79] The Department of Energy filed a memorandum in support of the United States Trustee's motion, contending that the Bankruptcy Code required the court to appoint an examiner because the DOE possessed an allowed, qualifying claim well in excess of $5 million.[80] The court nevertheless held that the appointment of an examiner under § 1104(c)(2) was not mandatory, for two reasons.[81]

First, the court appears to have had doubts that the DOE's claim satisfied the financial test. The claim apparently arose from a consent decree involving overcharges by the debtors.[82] Although more than $5 million in amount, it was not clear whether the debt qualified under the financial test, as the court apparently believed that the DOE was merely collecting on behalf of trade creditors.[83] While there were other creditors, they were banks holding claims that may or may not have been under-secured.

Second, and perhaps more important, the court reasoned that the legislative history failed to support the claim that appointment was mandatory. The mandatory appointment provision, the court explained, was intended to "satisfy the needs and dictates of a public company operating under the protections and laws of chapter 11."[84] The debtor in *GHR*, however, was privately held. After failing to find a "clear expression of why the mandatory examiner section was enacted," the court concluded an examiner was not required in all cases where there was greater than $5 million of non-trade debt.[85] The court denied the appointment because, in Judge Glennon's opinion, the costs would exceed the benefits.[86] "These Debtors are already ex-

an examiner by delay in seeking appointment); *In re* Shelter Res. Corp., 35 B.R. 304 (Bankr. N.D. Ohio 1983) (refusing examiner request as moot following settlement).

[78]*GHR,* 43 B.R. 165.

[79]43 B.R. at 167-68.

[80]*Id.*

[81]*Id.* at 170.

[82]*Id.* at 168, n.7 ("In fact, under the terms of the consent order and the confirmed plan of Refineries, the DOE's claim against Industries was allowed in the amount of $33,394,021.").

[83]*Id.* at 176 ("Finally, the Court believes that as to the claim of the DOE, it is not the kind of debt covered by [§ 1104(c)(2)]. The DOE claim arose in connection with overcharges made by the Debtors to purchasers of petroleum products.").

GHR illustrates practical problems with the $5 million financial test. The debtors had apparently failed to file schedules, so it was not clear whether there were sufficient qualifying unsecured claims. *Id.* at 167. Although it does not appear that public bondholders sought an examiner, several banks, which may or may not have been under-secured by more than $5 million, joined in the unsuccessful request. If the DOE had been asserting penalty or other non-tax and non-trade claims, they too would have qualified under a literal reading of the statute, notwithstanding the court's skepticism. Given these facts—and the fact that the debtors were privately held—the court's frustration with the text of the statute was not surprising.

[84]*Id.*

[85]*Id.* at 175.

[86]*Id.* at 176.

pending great sums of money to sustain the expenses of the professionals employed by the various parties-in-interest. . . . [t]he appointment of an examiner [was] neither prudent nor mandated."[87]

Courts remain suspicious of requests to appoint examiners, perhaps because they believe they are merely strategic ploys. Judge Gerber recently admonished the creditors' committee and the Office of the United States Trustee in the *Lyondell Chemicals* case for arguing that an examiner must be appointed if a case is large enough, no matter the consequences:

> I and the other bankruptcy judges around the country have seen the ways in which the mandatory appointment language has been abused. And it's obvious, to anyone with any large case experience, that mandatory appointment is terrible bankruptcy policy, and the Code should be amended, forthwith, to delete section 1104(c)(2), and to give bankruptcy judges (subject to appellate review, of course) the discretion to determine when an examiner is necessary and appropriate, and whether a request for an examiner is merely a litigation or negotiating ploy.[88]

In the seminal case supporting mandatory appointment, the Sixth Circuit in *In re Revco* held that § 1104(c)(2) required the appointment of an examiner when the financial test was satisfied.[89] The court considered the ordinary meaning of the word "shall," present in 1104(c)(2) but not found in 1104(c)(1), and held appointment to be mandatory.[90] Dismissing the debtor's dire predictions of abuse, the court noted that while the appointment of an examiner was outside its discretion, the scope of that appointment was not, including the nature, extent, and duration of examination.[91] In other words, while the Bankruptcy Code made appointment "mandatory" in the face of certain economic criteria, courts had flexibility to scale an examiner's actual role to fit the needs of a given case. Presumably, in extreme cases, an examiner could be appointed and yet given nothing to do and no budget with which to do it.

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[87]*Id.*

[88]*See Lyondell Transcript*, *supra* note 11, at 35. R

[89]*In re* Revco D.S., Inc., 898 F.2d 498, 499 (6th Cir. 1990).

[90]*Id.* at 501 ("Section 1104(b)(1) [now 1104(c)(2)], which governs the appointment of an examiner when the total unsecured debt is less than $5 million, follows the language of § 1104(a) [the appointment of a trustee]; in both cases the appointment is left to the bankruptcy court's discretion. The contrast with § 1104(b)(2) could not be more striking. When the total 'fixed, liquidated, unsecured' debt is greater than $5 million, the statute requires the court to appoint an examiner.").

[91]*Id.* ("[T]he bankruptcy court retains broad discretion to direct the examiner's investigation, including its nature, extent, and duration. Section [1104(c)] plainly states that the court shall appoint an examiner to conduct such an investigation of the debtor as is appropriate.'").

1.5 Recent Proposals and Reforms

Not surprisingly, there have been periodic calls to reform the Bankruptcy Code's provisions on examiners. In 2004, the Select Advisory Committee on Business Reorganization (SABRE), a committee established by the American Bar Association's Section of Business Law, Business Bankruptcy Committee, published its Second Report (SABRE Report), which included three explicit recommendations about the use of examiners, although none directly addressed the questions of when they should be sought or appointed.[92] First, the SABRE Report recommended that the Bankruptcy Code be amended to expand an examiner's powers to include explicitly the powers to object to claims, to prosecute causes of action on behalf of the estate, and to negotiate and conduct asset sales.[93] Second, it proposed to amend the Bankruptcy Code to empower an examiner to act as a "plan facilitator," to facilitate negotiations over a reorganization plan (and, if the negotiations failed, to propose a plan herself).[94] Third, it proposed to eliminate the obligation to file a report.[95] In essence, the SABRE Report sought to codify the notion of an examiner with "expanded powers," one who could explicitly do more than simply investigate and report on the debtor's failure.

The SABRE proposal has not been especially well received, due largely to the fact that it seeks to turn an entity that is generally expected to be "neutral" into one with a vested interest in certain outcomes under certain conditions.[96] Examiners are supposed to be "objective" and "disinterested," reporting, not advocating, the facts.[97] In part, this stems from a view that

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[92]*Second Report of the Select Advisory Committee on Business Reorganization*, 60 Bus. Law 277 (2004).

[93]*Id.* at 308.

[94]*Id.* at 310.

[95]*Id.* Bankruptcy § 1106(a)(4) currently requires an examiner to file a report of any investigation conducted under § 1106(a)(3) and to transmit a copy of the report to any creditors' committee, equity committee, any indenture trustee and any other entity as the court may direct. 11 U.S.C. § 1106(a) & (b).

[96]Kit Weitnauer, *Should an Examiner Prosecute Claims?*, 24 Am. Bankr. Inst. J. 50, 80 (2005) ("The primary concern this aspect of Proposal Three raises is its impact on an examiner's independence and integrity, or the parties' or the public's perception of an examiner's independence and integrity. The same concern exists where the courts have given examiners the power to prosecute claims").

[97]*See, e.g.*, *In re* Southmark Corp., 113 B.R. 280, 282, 284 (Bankr. N.D. Tex. 1990) ("While the court could direct that the appointed examiner use the services of the committee's court-approved accountant, that might defeat the objective of a disinterested examiner not associated with or serving creditors or equity security-holders . . . . [T]he court affirms the prior finding that the best interests of this estate compel the appointment of a disinterested, non-adversarial person with no connections to Southmark's creditors or equity security holders to investigate Southmark's pre-petition acts and conduct"); *In re* 1243 20th St. Inc., 6 B.R. 683, 686 (Bankr. D.C. 1980) ("The role of an examiner requires that he be disinterested. Accordingly, the objective statement rendered may be of immeasurable importance in determining those matters relating to vital aspects of the reorganization case").

examiners are fiduciaries not for the parties, but for the court itself.[98] According to one court, examiners should act as a "civil grand jury . . . to ascertain legitimate areas of recovery and appropriate targets for recovery."[99] They should be "amenable to no other purpose or interested party . . . ."[100]

Although the SABRE Report has not become law, Congress nevertheless has tinkered, indirectly, with the mechanics of examiner appointments. In 2005, Congress passed the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA). Clifford J. White III and Walter Theus, Jr. contend that BAPCPA created a new ground for the appointment of an examiner in addition to the two provided in § 1104(c).[101] BAPCPA added § 1104(a)(3):

> (a) At any time after the commencement of the case but before confirmation of a plan, on request of a party in interest or the United States trustee, and after notice and a hearing, the court shall order the appointment of a trustee—
>
> (3) if grounds exist to convert or dismiss the case under section 1112, but the court determines that the appointment of a trustee or examiner is in the best interests of creditors and the estate.

White and Theus predict that this BAPCPA provision may restore the mandatory nature of bankruptcy examiner appointments which, they claim, has slowly eroded since the passage of the Bankruptcy Reform Act of 1978.[102] This restoration would encourage "greater transparency in the bankruptcy process, more effective case administration, speedier and more comprehensive investigations of the financial condition of the debtor, and more expeditious resolution of the case."[103]

These and other claims about examiners are open to doubt. There has been no effort to understand the actual frequency of requests for, and appointments of, examiners. Nor has there been any systematic effort to understand what functions they perform. Answers to these questions will offer insight not only into the utility of examiners, but also the dynamics of chapter 11 reorganization. The balance of this paper addresses these questions.

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[98] *In re* Hamiel & Sons Inc., 20 B.R. 830, 832 (Bankr. S.D. Ohio 1982) (an examiner "constitutes a court fiduciary and is amenable to no other purpose or interested party . . . .").

[99] *Id.*

[100] *Id.*

[101] White & Theus, Jr., *supra* note 54, at 304 (2006). R

[102] *Id.* at 326.

[103] *Id.*

2. DESCRIPTIVE DATA

2.1 The Data

This study is based on hand-collected quantitative and qualitative data.

2.1.1 *Quantitative Data*

The quantitative data are a hand-collected dataset of 576 large chapter 11 cases commenced between 1991 and 2007. These cases are described in the Bankruptcy Research Database (BRD), which itself contains data on all large chapter 11 cases commenced under the current Bankruptcy Code.[104] Cases from the BRD are a good sample to evaluate the use of examiners for three reasons.

First, the BRD captures data about companies with assets in excess of $100 million and publicly traded securities that are the subject of cases under chapter 11.[105] These debtors all appear to have unsecured debts in excess of $5 million.[106] This is relevant because Bankruptcy Code § 1104(c)(2) provides that an examiner "shall" be appointed if "the debtor's fixed, liquidated, unsecured debts, other than debts for goods, services, or taxes, or owing to an insider, exceed $5,000,000."[107] While examiners may be appointed in smaller cases, the size of these debtors suggests that the appointment of an examiner would be required in all (or almost all) of these cases—if sought and if one views the language of the statute as mandatory.

Second, the debtors in these cases have publicly traded securities. As discussed above, the role of the examiner (and in particular the mandatory appointment in certain "large" cases) was created in part from concern for protecting public debt investors. Prior to enactment of the current Bankruptcy Code, the SEC at least in theory played a larger role in the reorganization of companies with publicly traded securities and would presumably have protected investors. Current law largely eliminated that function. It appears that examiners were expected to pick up some of this slack.

Third, because they involve "large" companies (those with scheduled assets in excess of $100 million), the debtors in these cases likely have cash flow

[104] *See* discussion at note 24. R

[105] *See* Bankruptcy Research Database – Contents, http://www.webbrd.com/contents_of_the_webbrd.htm (last visited Sept. 16, 2009).

[106] I have not independently verified the amounts indicated in the BRD. Further, I have assumed based on case size, and the available data, that all or most cases drawn from the BRD have at least $5 million in qualifying unsecured claims under § 1104(c). I base this assumption in part on the fact that in no case were scheduled liabilities less than $21 million. While some of this debt will likely be "non-qualifying" trade or tax debt, as the discussion of the *GHR* case, *supra,* makes clear, a debtor may have large amounts of unsecured debt owed to banks, to holders of privately placed notes, or for other non-trade, non-tax claims. The important question is not so much the real amount of qualifying unsecured debt as the perception at the time that a debtor probably had such debts. It is this perception that seems most likely to matter to those who assert that an examiner must be appointed in large cases.

[107] 11 U.S.C. § 1104(c)(2).

sufficient to support the cost of an examiner. Moreover, being large cases with publicly traded securities, they are more likely to have the "great public interest"[108] that Congress thought relevant to the role of the examiner.

These cases are thus not representative of all chapter 11 cases. At most, they are representative of the largest of chapter 11 cases. While future studies may analyze the use of examiners in smaller chapter 11 cases, the cases in the BRD likely provide the best available opportunity to understand cases in which examiners are most likely to be sought and appointed.

The 576 cases sampled from the BRD were all cases in that dataset (i) commenced between January 1991 and June 2007, inclusive,[109] and (ii) for which I could obtain dockets and/or pleadings.[110] The BRD itself does not contain information on the use of examiners (or related matters). Thus, the data from the BRD were supplemented with hand-collected data on the use of examiners (and related matters) from the dockets (and in certain cases, pleadings) for these cases. This set of 576 cases is referred to as the "Examiners Database."

The Examiners Database uses cases from 1991 to 2007 for two reasons. First, far fewer dockets are available for BRD cases prior to 1991.[111] Second, as discussed above, the only circuit-level decision on the use of examiners—*Revco*—was decided in 1990, confirming (at least for the Sixth Circuit) that the appointment of an examiner is mandatory when a debtor has more than $5 million in qualifying unsecured claims.[112] 1990 thus forms a sensible break point, although it precludes a more complete historical analysis, which others may wish to undertake as older dockets come online.

The data in the Examiners Database were collected, recorded, and analyzed in three basic steps.

First, I obtained dockets for all cases in the Examiners Database, almost all through PACER.[113] I searched the dockets for entries using the word

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[108]124 CONG. REC. S 17403-34 daily ed., Oct. 6, 1978 (*reprinted in* COLLIER, App. 14.4(f)(iii) (15th ed. Rev 2002)) (statement of Senator DeConcini).

[109]The BRD was provided in an Excel spreadsheet. The information contained in the BRD as received has not been independently verified.

[110]For 45 of these cases, some or all of the relevant pleadings were also obtained, including motions requesting or opposing the relief sought, orders entered with respect to such relief, and reports filed.

[111]Of the 618 cases in the BRD from 1991 to 2007, I have dockets for 596 (96.4%) cases—549 (88.8%) full dockets, 20 (3.2%) partial dockets, and 27 (4.4%) pending dockets—and pleadings for 47 (7.6%) cases. By comparison, of the 118 cases in the BRD prior to 1991, I have dockets for 60 (50.8%), and pleadings for none.

[112]*In re* Revco D.S., Inc., 898 F.2d 498, 501 (6th Cir. 1990).

[113]Mining PACER for data about trends in practice is an increasingly popular undertaking with academics. *See, e.g.*, Christina L. Boyd & David A. Hoffman, *Disputing Limited Liability*, 104 NW. L. REV. __ (forthcoming 2009) (collecting and analyzing longitudinal data from PACER on veil piercing claims); David L. Schwartz, *Practice Makes Perfect? An Empirical Study of Claim Construction Reversal Rates in Patent Cases*, 107 MICH. L. REV. 223 (2008) (using PACER to create database of patent cases); James D.

"examiner," or variations thereof, and variations of "Bankruptcy Code § 1104." This produced two classes of cases: (i) those involving the sorts of examiners studied here (i.e., appointed under Bankruptcy Code § 1104), and (ii) so-called "fee examiners" occasionally appointed to review the fees sought by professionals in large bankruptcy cases. Because fee examiners have little to do with the mandate of "real" examiners[114] those cases did not count as examiner cases (unless a § 1104 examiner was also sought in the case[115]).

Second, I searched the dockets for entries involving the use of the words "chapter 11 trustee" or similar import (again, using wildcards as appropriate). A chapter 11 trustee may be appointed under Bankruptcy Code § 1104(a) for grounds that overlap in important respects with the grounds that might give rise to the appointment of an examiner (e.g., fraud, dishonesty, or management incompetence).[116] It is, however, generally believed that the appointment of a chapter 11 trustee has far more severe consequences than the appointment of an examiner. Unlike an examiner, a chapter 11 trustee presumptively will run the debtor's business and thus displace management.[117] Moreover, chapter 11 trustees may be more expensive than examiners, as they are paid a "reasonable" fee capped at a percentage of assets distributed by the estate, rather than a fixed hourly fee.[118] In other words, chapter 11 trustees and examiners may be responses to similar problems, but they are not substitutes for one another. Indeed, some system participants interviewed for this project indicated that they believed that examiners were ap-

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Cox, Randall S. Thomas and Lynn Bai, *There Are Plaintiffs and . . . There are Plaintiffs: An Empirical Analysis of Securities Class Action Settlements*, 61 VAND. L. REV. 355 (2008) (using PACER to study securities class action disputes).

[114]*See* Lubben, *supra* note 23 (discussing role of fee examiners). R

[115]Both fee examiners and § 1104 examiners were sought in six cases, including *Adelphia Communications*, *Polaroid Corp.* and *U.S. Airways* (2002).

[116]Bankruptcy Code § 1104(a) provides in pertinent part:

> (a) At any time after the commencement of the case but before confirmation of a plan, on request of a party in interest or the United States trustee, and after notice and a hearing, the court shall order the appointment of a trustee—
>
> (1) for cause, including fraud, dishonesty, incompetence, or gross mismanagement of the affairs of the debtor by current management, either before or after the commencement of the case, or similar cause, but not including the number of holders of securities of the debtor or the amount of assets or liabilities of the debtor; or
>
> (2) if such appointment is in the interests of creditors, any equity security holders, and other interests of the estate, without regard to the number of holders of securities of the debtor or the amount of assets or liabilities of the debtor.

11 U.S.C. § 1104(a).

[117]Bankruptcy Code § 1108 provides that "[u]nless the court, on request of a party in interest and after notice and a hearing, orders otherwise, the trustee may operate the debtor's business." 11 U.S.C. § 1108.

[118]*See* 11 U.S.C. § 326.

pointed as a less severe alternative to a request for the appointment of a chapter 11 trustee. To some extent, and as discussed below, the docket-level data support this observation.

Third, I searched the dockets for entries involving motions to convert a case to a chapter 7 liquidation, or to dismiss the case entirely (again, using wildcards as appropriate). Both conversion and dismissal are governed by Bankruptcy Code § 1112, which provides that such relief may be granted if there is, among other things, "gross mismanagement" of the bankruptcy estate.[119] Conversion or dismissal is potentially the most draconian act a bankruptcy judge could take in a case, as it effectively ends the reorganization effort, either causing the company to be liquidated immediately (or in very short order) or the case to be dismissed entirely, leaving the debtor's fate to other fora.[120]

Conversion or dismissal may thus be seen as forming one end of a continuum of relief for serious problems that might afflict a chapter 11 debtor or its case. At the other end will be the examiner, the principal object of this study. Yet, because similar grounds—e.g., incompetent management—could lead to any of these three forms of relief (examiner, trustee, or conversion/dismissal), I coded for all three.

With respect to examiners, I reviewed dockets to determine: (1) whether a request for any of these three forms of relief was made; (2) if so, who sought it; (3) the basis for the request; (4) whether any party objected; (5) if so, who objected; (6) whether the relief was granted; (7) if an examiner was appointed, what he or she did (where that information was available); (8) whether the request was explicitly denied; (9) whether the request was withdrawn; and (10) whether the request appears effectively to have been denied by having been mooted by the occurrence of a subsequent event, such as the confirmation of a plan or appointment of a trustee.

With respect to trustees and motions to convert or dismiss the case, dockets were reviewed to determine whether requests were made and/or granted.

Further information about how I gathered the quantitative data appears in Appendix 1.

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[119] *See* 11 U.S.C. § 1112. This provision provides, in substance, that a case may be converted or dismissed, "whichever is in the best interests of creditors," provided there is "cause" to do so. *Id.* § 1112(b)(1). "Cause" includes "substantial or continuing loss to or diminution of" the value of the estate or "gross mismanagement of the estate." *Id.* at § 1112(b)(1)(A) & (B).

[120] Conversion or dismissal motions may not always signify serious problems. Of 60 cases in which a conversion or dismissal motion was granted, 17 also involved confirmed plans. In some cases (*Genesis Health Ventures* (00-02692), for example), dismissal occurred after a plan was confirmed. Moreover, 99 cases resulted in confirmed plans even where a motion to convert or dismiss was made. Nevertheless, plans were not confirmed in forty-two cases in which a conversion or dismissal motion was made or granted.

2.1.2 *Qualitative Data*

I supplemented the quantitative data in the Examiners Database with qualitative data from structured interviews with bankruptcy lawyers, judges, examiners, and other system participants. The interview participants were found through a mass email sent to all attorneys for whom I could obtain email addresses and whose names appeared in the BRD, as well as other participants to whom I was referred. In total, 19 interviews were conducted, all by the author. Although four were recorded and transcribed, other participants declined to permit the interviews to be recorded, in which case I took contemporaneous notes. All participants requested that their identities remain anonymous.[121] Further information about the interviews appears in Appendix 2.

2.2 Descriptive Data

In order to understand when examiners are likely to be sought or appointed, and what they do, it is useful to understand the characteristics of the cases and companies in which they are involved, as well as substantially similar cases and companies in which they are not. This part describes the cases and companies in the Examiners Database.

2.2.1 *Court, Case and Company Characteristics for Sample*

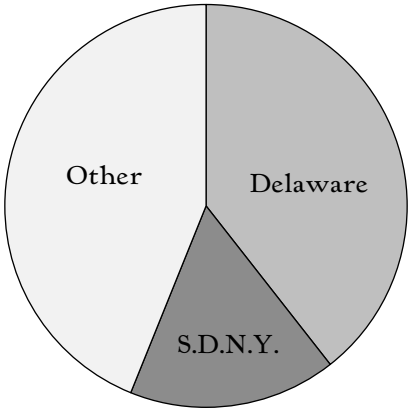
The 576 cases in the Examiners Database were from 54 different judicial districts, filed at an average rate of 33.88 cases per year. The peak years for case filings were 2001 and 2002, with 97 (about 16.8%) and 81 (about 14%) filings, respectively. The bulk of the cases (323, or 55.9%) were filed in the bankruptcy courts of one of two "big" districts, Delaware (227 cases, or 39.4% of cases) and the Southern District of New York (96 or about 16.6% cases).

The vast majority of cases in the Examiners Database were voluntary (551 or 95.7%). Reorganization plans were confirmed in 489, or about 81.6%. The plans were "prepackaged" in 163 (or 28.3% of) cases. Chapter 11 trustees were appointed in 24 cases or about 4.2%, and motions to convert or dismiss were granted in 59 cases (10.2%). The average time spent in chapter 11 was 13.9 months. Fifty-three companies refiled after emerging from bankruptcy, for a refiling rate of about 14% (n=380).

All debtors in the sample are "large," meaning they had assets in excess of $100 million. Debtors in the sample had median (mean) scheduled assets of

[121] In order to keep track of the interviews, and to identify the roles the subjects play in the system, the citations are in the following form: [ROLE]-[SUBJECT NUMBER]. There were four categories of interview subjects, whose roles were abbreviated as follows: (1) Lawyers (L), (2) Judges (J), (3) Examiners (E), and (4) Other system participants (e.g., administrators, investors) (O). Thus, a citation to an interview with the first lawyer interviewed would be "L-1." Redacted copies of the notes and transcripts are available on request.

Figure 2.2.1—Filings in "Big" Districts (SDNY and Delaware) and Other Districts



$512 million ($2.03 billion) (*n*=358), respectively, and median (mean) scheduled liabilities of $558 million ($2.12 billion) (*n*=258).[122]

2.2.2 *Court, Case and Company Characteristics for Examiner Cases*

As noted above, motions for and appointments of examiners are fairly rare. Examiners were sought in a total of eighty-seven (15.1% of) cases in the Examiners Database and appointed in thirty-nine cases (about 6.7%). Table 2.2.2 (attached[123]) contains a list of the cases in which an examiner was sought or appointed, the district and year of the case, and the name of the examiner, if known. Examiner requests and appointments peaked in 2002, the same time as filings for the entire sample.

The fact that examiners are rare does not, however, necessarily mean that

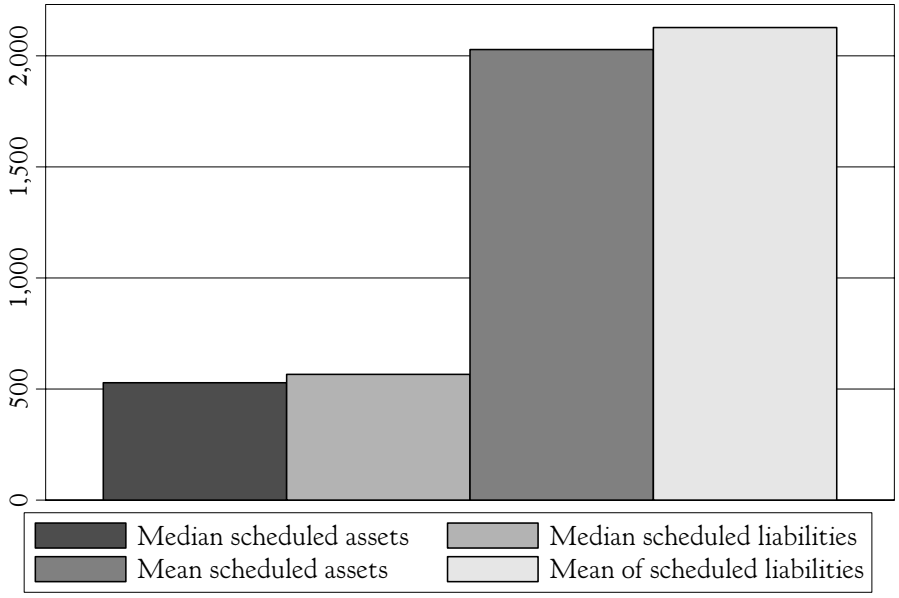
[122]I will tend to report median financial values before means because, as discussed further below, the financial data skew heavily in this regard, due to several very large outliers. Medians tend to present a more accurate picture of these data. I also note that the available financial data were somewhat limited, with only 358 observations of scheduled assets and 258 observations of scheduled liabilities for companies in the Examiners Database.

In order to address this, I also analyzed financial data from other sources, in particular assets as reported on the last Form 10-K filed before bankruptcy and total liabilities reported by Compustat for the year preceding the bankruptcy. *See* Wharton Research Data Services, http://wrds.wharton.upenn.edu/ds/comp/tools/finstateextract.shtml (last visited Feb. 25, 2010). As discussed in Part 3, 10-K reported assets had a slightly lower mean ($2.011 billion) and slightly higher median ($554 million) than did scheduled values (*n*=576).

Notwithstanding missing values, I generally used scheduled amounts rather than amounts reported elsewhere for two reasons. First, scheduled amounts would have been stated more closely to the time of the bankruptcy filing (indeed, at or after commencement of the case), and thus should have presented a picture that appeared, at the time, to be more "accurate." Second, after running a variety of tests discussed further in Part 3, results based on scheduled values versus those obtained from other, comparable financial data generally provided no greater statistical power than did scheduled values.

[123]Longer tables are attached to the end of this paper; shorter ones appear in text.

Figure 2.2.1-A Financial Statistics of Debtors in Sample ($ millions)



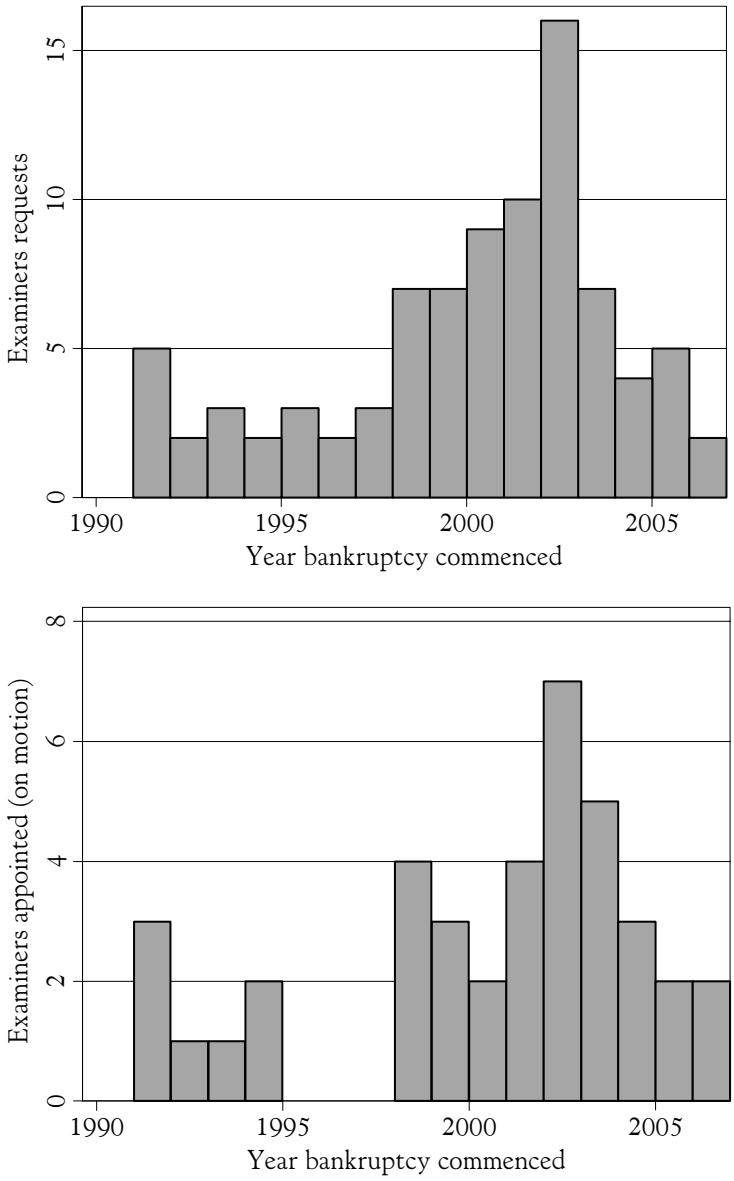
courts actually denied requests for examiners. Rather, a review of the dockets indicates that courts entered orders explicitly denying a motion to appoint an examiner only seventeen times (or 21.5% of requests). In twelve cases where an examiner was requested, the court simply took no action at all (about 15% of cases with examiner requests).[124] In other cases, the court may have taken no action because the motion became moot (sixteen times). The motion may have been rendered moot by virtue of the confirmation of a plan of reorganization (thirteen times), or the appointment of a trustee (twice), or because the movant's claim was settled (once). In fourteen cases an examiner was not appointed because the movant withdrew the motion.[125] It is not possible to know why examiner motions were withdrawn, although it is likely that the movants were given some reason to do so (e.g., information about the case or a favorable settlement).

Most requests for examiners came from one of two "big" districts, Dela-

[124]That is, cases where the court did not grant or deny the request. I treated these as denials (although not affirmative denials) because an examiner appointment would likely result in additional docket entries involving the examiner, including applications to retain professionals, perhaps requests for (and oppositions to) discovery, reports, and, of course, fee applications. The absence of such pleadings in an otherwise apparently complete docket creates a reasonable inference that no examiner was appointed.

[125]The numbers do not total to 45 requests denied because a request may have been withdrawn and rendered moot in the same case. I did not treat those as alternatives because withdrawal was inherently interesting, and in some cases co-extensive with mootness (i.e., the plan is confirmed and the request is withdrawn at approximately the same time).

Figure 2.2.2: Examiner Requests and Appointments



ware (twenty-seven, or 31% of requests) or the Southern District of New York (nineteen, or 21.8%). Although most requests occurred in these big districts, that is not where most examiners were appointed. Collectively, courts in big-district cases appointed only seventeen examiners (eight in Delaware and nine in the Southern District of New York), or 40.5% of appointments, as

compared to twenty-five appointments in the other, "non-big-district" cases (59.5%).

Most cases in which an examiner was requested (eighty-three of eighty-seven or 95.4%) were voluntary. Cases in which examiners were requested and appointed were slightly more likely to result in confirmed reorganization plans (about 94% for cases with examiner requests or appointments) than the sample as a whole (83.7% confirmation rate). Sixteen cases in which an examiner was requested (18.3% of requests) used prepackaged plans.

Cases in which an examiner was sought or appointed lasted longer (16.9 and 19.6 months, respectively) than cases where no examiner was sought (13.9 months, as noted above). Cases in which an examiner was sought were about as likely to refile as cases in which no examiner was sought (about 14% each). Cases in which an examiner was actually appointed, however, were almost half as likely to result in refiling, 8% as compared to the refiling rate of 14% for the entire sample.

As explained in Part 1, examiners may be a form of relief less drastic than the appointment of a trustee or the conversion or dismissal of a case. Data about these events were collected for cases in the Examiners Database because they may be responses to similar problems (e.g., fraud or mismanagement). Examiners were sought slightly more frequently (15.1% of cases) than requests to appoint a chapter 11 trustee (14% of cases). However, far more cases (about 25%) had at least one motion to convert the case to one under Chapter 7 or dismiss it.[126] Table 2.2.2-A (below) summarizes the number of cases in which these three forms of relief (examiner, trustee, conversion/dismissal) were sought and granted.

Table 2.2.2-A: Frequency of Types of Relief Requested/Granted

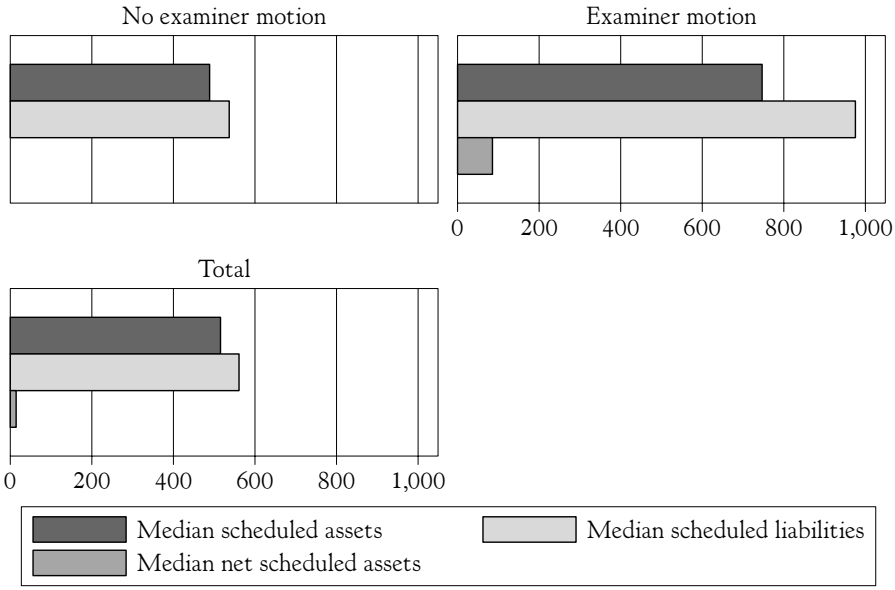
		All Cases	
		Cases	*% All*
All Cases		576	100%
Examiner	*Requested*	87	15.1%
	Granted	39[127]	6.77%
Trustee	*Requested*	81	14.06%
	Granted	24	4.17%
Conversion or Dismissal	*Requested*	147	25.52%
	Granted	59	10.24%

[126]In 96 cases, it appears motions to convert or dismiss were filed notwithstanding confirmation of a plan, of which seventeen were granted. This suggests that in some cases, such motions may have been ministerial in nature, and not a reflection of a more serious problem in the case.

[127]As noted elsewhere, examiners were appointed in three cases where it appears no motion was filed.

Median scheduled assets in cases in which an examiner was sought were almost twice as large as the sample. Mean scheduled assets in cases with an examiner motion were more than four times larger than the sample. Companies for which an examiner was sought by motion listed scheduled median (mean) assets of about $750 million ($5.6 billion) (*n*=60), as compared to $489 million ($1.3 billion) for cases in which no such motion was made, and $512 million ($2.03 billion) for the entire sample (*n*=358). Similarly, cases in which an examiner was sought had median (mean) liabilities of $974 million ($4.85 billion) (*n*=44), as compared to $534 million ($1.55) (*n*=214) for companies in which no such motion was made, and $557 million ($2.12 billion) for the entire sample (*n*=258). Cases in which an examiner was sought had median (mean) net scheduled assets of $79 million ($2.16 billion) (*n*=43), as distinct from $500 (-$348) thousand for cases in which no motion was made, and $13 ($364) million for the entire sample.

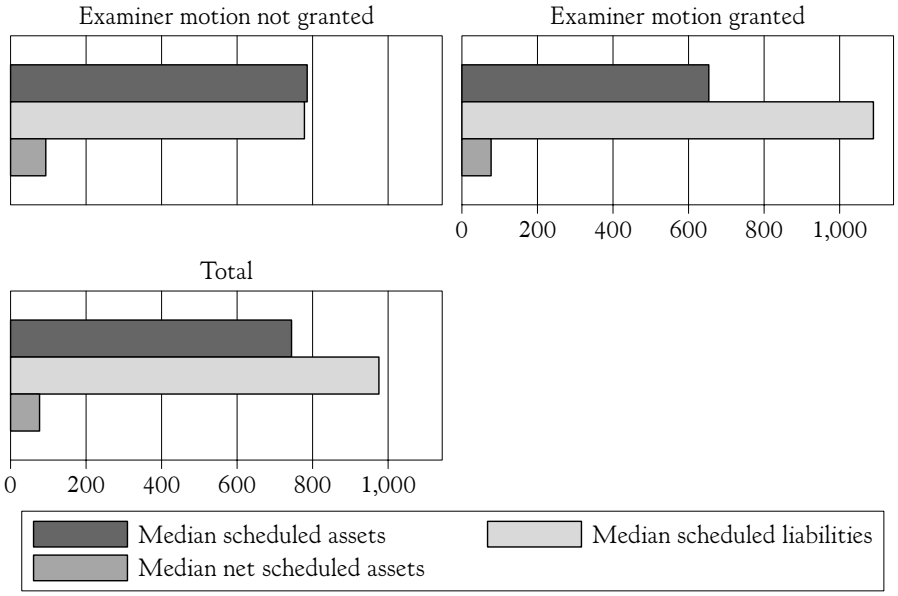
Figure 2.2.2-B Financial Statistics: Examiner Motions ($ millions)



Cases in which an examiner motion was granted were actually smaller by median assets than cases where the motion was not granted; they were, however, larger by mean assets. Companies in which an examiner was appointed on motion had median (mean) scheduled assets of $649 million ($8.65 billion) (*n*=28), as compared to $780 million ($3.02 billion) (*n*=32) for cases where the motion was not granted. Cases in which an examiner motion was granted had median (mean) liabilities of $1.08 billion ($6.7 billion) (*n*=21), as

compared to $775 million ($3.15 billion) (*n*=23) for cases in which the motion was not granted. Cases in which an examiner motion was granted had median (mean) net assets of $76 million ($4.8 billion) (*n*=20) as compared to net assets of $95 million (-$163 million) in cases where the motion was not granted (*n*=23).

Figure 2.2.2-C Financial Statistics: Examiner Appointments ($ millions)[128]



NewPower Holdings was the smallest case by liabilities in which an examiner was sought (and, coincidentally, appointed), with about $78 million in scheduled liabilities.[129] By scheduled assets, the smallest case in which an examiner was sought had $1.5 million (*Envirodyne*);[130] the smallest in which an examiner was actually appointed (*United Airlines*) had $84 million in assets.[131]

The largest case, by scheduled liabilities, in which an examiner was requested (and, coincidentally, appointed) was *Refco*, which listed liabilities of $48.6 billion.[132] The largest case, by assets, in which an examiner was requested (and, coincidentally, appointed) was *Worldcom,* which scheduled as-

[128]The table does not reflect three sua sponte appointments.

[129]*In re* New Power Holdings, Inc., No. 02-10835 (Bankr. N.D. Ga.).

[130]*In re* Envirodyne Indus. Inc., No. 93 B 319 (Bankr. N.D. Ill). Although this company's schedules listed less than $100 million in assets, its 10K before bankruptcy showed that it had over $1 billion in assets, which is why it appears in the Bankruptcy Research Database (and thus the Examiners Database).

[131]*In re* UAL Corp. (United Airlines), No. 02-48191 (N.D. Ill).

[132]*In re* Refco Fin., Inc., No. 05-60006 (Bankr. S.D.N.Y).

sets of $107 billion.[133]

The largest case, by both assets and liabilities, in which an examiner was neither sought nor appointed was *Conseco*, listing assets of $52.2 billion and liabilities of $51.7 billion. The smallest case, by both assets and liabilities, in which an examiner was not sought was *Liberate Technologies*, with $257 million scheduled assets, and $21.7 million in scheduled liabilities.[134]

2.2.3 *Who Requests Examiners?*

Bankruptcy participants interviewed for this project indicated a belief that particular types of parties had predictable positions with respect to requests for examiners and related relief. A refrain was that neither the Unsecured Creditors Committee (UCC) nor the debtor in possession (DIP) would likely seek an examiner. Instead, those interviewed frequently indicated that they would expect that those entities would oppose such requests. The UCC would resist because an examiner would interfere with the UCC's investigative function.[135] The DIP would do so because an examiner would interfere with management's prerogative to reorganize the debtor. Rather, if Congress believed the examiner would benefit the "investing public," then we would expect to see requests for examiners coming chiefly from individual investors and not from the UCC, the DIP, or other constituencies.

In fact, individual investors were not especially likely to request an examiner, making only eighteen of the eighty-seven examiner motions filed.[136] Rather, the parties most likely to request an examiner were creditors, either individually (thirty-two requests)[137] or via the UCC (fifteen requests).[138] Official Committees of Equity Holders only sought examiners four times. The government (in particular, the United States Trustee) moved or supported an examiner motion sixteen times. Even the DIP asked in two cases.

As important as knowing who asks for an examiner is knowing whether the request was opposed and, if so, who opposed it. An examiner motion was

[133]*In re* Worldcom, Inc., No. 02-13533 (Bankr. S.D.N.Y.).

[134]*In re* Liberate Techs., 04-11299 (Bankr. D. Del.).

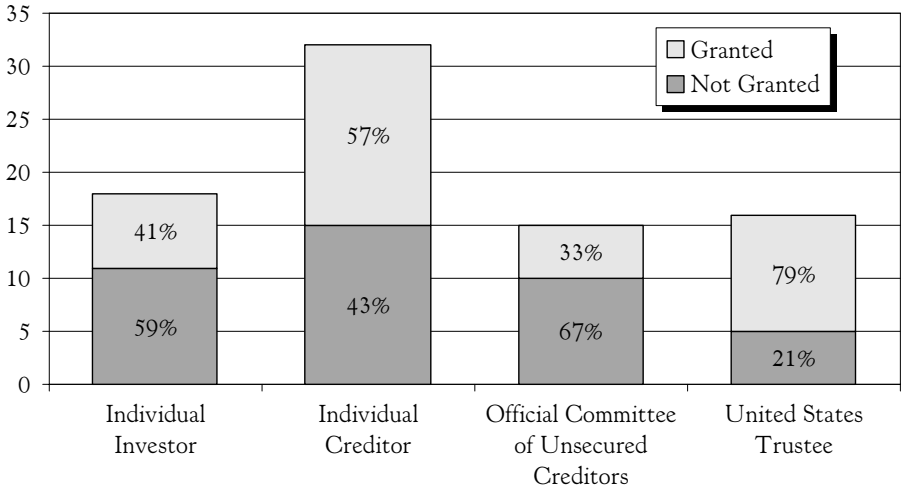
[135]Bankruptcy Code § 1103(c)(2) provides that, among other things the UCC may "investigate the acts, conduct, assets, liabilities, and financial condition of the debtor, [and] the operation of the debtor's business . . . ." 11 U.S.C. §1103(c)(2).

[136]Individual investors were coded as such if, from the docket or the pleadings, it appeared that the movant had purchased securities (equity or debt) of the debtor or claimed to be a plaintiff in securities fraud litigation involving the debtor.

[137]Individual creditors were coded as such if, from the docket or the pleadings, it appeared that the movant was a creditor and indicated that the basis for its claim did not involve the purchase of securities but was instead debt for services rendered or goods sold or leased.

[138]In some cases, multiple parties would request an examiner, or would file motions "joining" in the request. Because I am interested in identifying who asks for an examiner, I treated each party individually, meaning any request or joinder motion would be treated as a motion "for" an examiner, even if more than one party made such a motion in a given case. Thus, there will be more requests here than the total of requests on a per-case basis.

Figure 2.2.3: Examiner Appointment by Requesting Party



opposed by at least one party in fifty-nine (or about 70%) of the eighty-seven cases where requested. Not surprisingly, the DIP opposed in forty cases, and the UCC opposed in thirty cases. The most frequent grouping of objectors was the DIP and the UCC, who together objected in twelve cases, or 20% of cases in which an objection was filed. Interestingly, the government also opposed the appointment of an examiner in six cases. Equally interesting, however, was the fact that no opposition was filed at all in twenty-six cases (about 30% of cases where an examiner was sought).

Although examiner requests were frequently opposed, the objections were not terribly successful. Examiners were appointed notwithstanding an objection in twenty-nine cases, or about 76% of the thirty-nine cases in which an examiner was appointed on motion.

2.2.4 *The Costs of Examiners*

Those interviewed for this study frequently indicated that cost was an important concern in deciding whether an examiner was appropriate for a case. A review of cases for which fee data could be obtained (n=27) indicates a wide variation in the expenses associated with an examiner, ranging from about $18,000 to more than $250 million, with a mean cost of $15.1 million. Consistent with the marked role of outliers in examiner cases, this number is somewhat misleading, as the median cost was about $280,000.

3. FACTORS THAT AFFECT EXAMINER APPOINTMENTS

This paper considers when examiners will be sought and appointed in large chapter 11 cases. Many factors might matter, including these:

- *Economics*: The descriptive data above indicate that cases where examiners are sought and appointed are generally larger than cases where they are not. Those interviewed for this paper suggested that courts will engage in a cost-benefit analysis when considering whether to appoint an examiner taking account of, among other things, the debtor's financial condition. How do economics influence the presence of examiners?
- *Venue*: A long-standing debate among bankruptcy academics asks whether courts with the largest cases, economically speaking (those in the Southern District of New York and Delaware), defer excessively to management of a debtor and/or counsel for the main participants in the case.[139] If these courts wish to protect managers and professionals, they may be reluctant to appoint examiners. We know from the descriptive data discussed above that, even though courts in "small" districts get fewer examiner motions, they grant them somewhat more frequently. Does venue associate with examiner requests or appointments?
- *Context*: Various contextual factors might matter in the use of examiners. The Bankruptcy Code explicitly treats fraud as a basis for appointing one. Those interviewed for this paper indicated a belief that examiners may be sought and appointed in cases involving failures in the expected negotiating dynamics. The descriptive data suggest that examiner cases may be longer, more complex and more contentious than cases in which an examiner is not sought or appointed. Do these and similar contextual factors influence the presence of examiners?

This Part aims to detect which factors were associated with examiner requests or appointments.

3.1 Methodology and Qualifications

Before developing the inferential analysis, I describe the methodology and its limitations.

In univariate analysis, two-sample t-tests were used for comparisons between the means of the groups (e.g., the mean number of debtors in each group), and Wilcoxon non-parametric tests were used to test the difference of medians (due to the skewness of the distributions).[140] Pearson's chi-squared tests (X^2) (or Fisher's exact tests when cell sample size was small)[141] were

[139]*See* LoPucki, Courting Failure, *supra* note 23. R

[140]This is a non-parametric test of significance between two groups (e.g., the assets or liabilities of cases with and without a request for an examiner). *See generally* G.W. Corder & D.J. Foreman, Nonparametric Statistics for Non-Statisticians: A Step-by-Step Approach (Wiley 2009).

[141]See R.A. Fisher, *On the interpretation of* X^2 *from contingency tables, and the calculation of P*, 1 J. Royal Stat. Soc. 85, 87-94 (1922).

used to test the association of categorical variables (e.g., whether or not the case involved allegations of fraud) with the outcomes of interest.

Factors that were trending significant from univariate analysis (p-value<0.05) were subsequently added to a logistic regression model to predict the likelihood that an examiner would be requested. Factors that were retained for this analysis included: (1) assets (as listed in the bankruptcy schedules and reported on Form 10-K); (2) liabilities (as scheduled); (3) net scheduled asset values; (4) whether the case was filed in a "big district" (Delaware or the Southern District of New York); (5) allegations of fraud; (6) days in bankruptcy; (7) docket counts; (8) motions to appoint a trustee; and (8) the use of a prepackaged plan.[142] To predict examiner appointments, I used the foregoing plus the presence of an examiner motion.

In order to account for the skewed distribution of continuous variables and to make the data more easily interpretable, I recoded cases involving scheduled net assets into three categories: (1) those with net negative assets; (2) those with net assets between $0 and $100 million; and (3) those with net assets in excess of $100 million. I also recoded scheduled liabilities into three categories: (1) cases with liabilities less than $558 million; (2) those with liabilities between $558 million and $1.5 billion; and (3) those with liabilities exceeding $1.5 billion. I chose these groupings for two reasons. First, they tend to modulate the skewness of these data (especially as to liabilities). Second, these groupings help to focus the analysis on important economic questions, in particular whether examiner motions associate with a debtor's observable financial condition (e.g., positive asset valuations or liabilities, the "mandatory" criterion chosen by Congress).

I coded the Form 10-K assets into equal quartiles as follows: (1) those with less than $322 million; (2) those between $322 and $554 million; (3) those between $554 million and $1.3 billion; and (4) those above $1.3 billion. I similarly coded dockets into equal quartiles: (1) those with fewer than 734 entries; (2) those between 734 and 1617 entries; (3) those between 1617 and 3140 entries; and (4) those with greater than 3140 entries. Trustee and conversion or dismissal motions were treated as standard categorical variables (filed or not filed).

Only factors that remained significant in the multivariable model were retained to maximize power in the most parsimonious model possible. Finally, I also tested for interactions based on an *a priori* hypothesis that the influence of net asset values on examiner motions might be modified by whether a case had a trustee motion.

A word of caution is in order. This study would ideally provide a model

[142]There is no purpose to testing the effect of plan confirmation since, by statute, an examiner could not be appointed after a plan was confirmed. *See* 11 U.S.C. § 1104(c)(2).

that predicted with certainty the factors that will lead to both requests for, and the appointment of, examiners. Unfortunately, while the available data make it possible to predict when examiners will be requested, it is less clear when those motions will be granted, for three reasons.

First, examiners are not sought frequently. As noted in Part 2, of 576 cases in the Examiner's Database, they were sought in only eighty-seven cases, and those requests were granted in only thirty-nine cases (in addition, as noted, I found examiners appointed in three cases without any docketed motions, suggesting they were appointed *sua sponte*[143]). The infrequency of this dependent variable reduces statistical power. I cannot say with certainty when an examiner will actually be appointed, although the data do suggest certain trends (and the request for examiner motions is certainly on the causal pathway).

Second, certain continuous variables—in particular financial and docket entry data—are not normally distributed. Here, the means tend to be much higher than the medians because, as noted in Part 2, above, there are huge outliers in the sample and especially among the cases in which examiners were sought and appointed.

Third, inferences might be biased by the absence of scheduled asset and liability values. As noted above, the Examiners Database contains only 358 and 258 observations of each, respectively. It is difficult to know in any given case why scheduled asset and liability amounts are missing. These data come from the Bankruptcy Research Database (BRD) and were not hand-collected for this paper. They may be missing from the BRD for any number of reasons, including that companies failed to file required schedules; companies did file them, but without this information; or the data were simply not collected by the BRD.

In order to determine whether the absence of scheduled financial values biased the analysis, I took two steps. First, I analyzed outcomes using Form 10-K asset values, which the BRD also reports. Unlike scheduled values, however, the BRD (and thus the Examiners Database, which incorporates these variables from the BRD) has a full set of asset observations based on the Form 10-K filings (n=576). The range of Form 10-K asset values is roughly similar to the range of scheduled asset values, suggesting that cases without scheduled asset values are likely to be similar (for this purpose) to cases with those values.[144] A rank-sum test of either variable shows a statistically significant association with examiner motions.[145]

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[143]*Baldwin Builders* (95-13057), *El Paso Refinery* (94-30051), and *Bonneville Pac. Corp.* (91-27701).

[144]Cases in the Examiners Database had median (mean) Form 10-K asset values of $554 million ($2.011 billion) (n=576) as compared to scheduled assets of $512 million ($2.028 billion) (n=358).

[145]A Wilcoxon rank-sum test of Form 10-K assets for examiner motions shows significance at $p<0.00$; the same test of scheduled assets also shows significance at $p=0.024$.

Second, I considered whether there was an association between examiner motions and cases without scheduled financial information. This is an appealing theory if we believe that examiners exist to fill informational gaps when a company goes into bankruptcy. It is easy to imagine that accurate financial information is important to those involved in the reorganization. If it is missing, the appointment of an examiner might be a sensible way to get it. In fact, however, cases with requests for examiners and actual appointments (including *sua sponte*) are *more* likely to have scheduled financial information than cases in which an examiner was not sought. There is thus no statistically significant association between the absence of this information and a request for an examiner.[146]

I believe the absence of data does not bias the results. Nevertheless, sample size, skewed distributions and missing data across certain variables all present challenges to producing a robust analysis of the various factors that appear to lead to an examiner appointment and to determining how factors interact to influence this outcome. At one level, this is not surprising. Because many suspect that examiners are often sought for strategic reasons—and not the more legitimate investigative purposes envisioned by Congress—it may be that the factors that lead judges to deny motions (or let them become moot) reflect concerns that cannot be observed in the data. Real or perceived strategic behavior across a small number of cases may be the (unobservable) factor that deprives us of the ability to know when (in a statistically valid way) examiner requests will be approved.

At the same time, there is an obvious correlation between a request for an examiner and an examiner's appointment, and the two are on the same causal pathway.[147] Except for three cases noted above, examiners were always appointed on written motion. It is therefore reasonable to infer that the factors relevant to examiner requests are also relevant to examiner ap-

Given their similarity, I did not use the Form 10-K values exclusively because they are not likely to be as reliable or influential on case participants as scheduled values. Form 10-K values are likely less reliable than scheduled values because, among other reasons, they preceded bankruptcy, may not have reflected write-downs in assets prior to bankruptcy and, in any case, were less likely to be the values observed and considered by the parties and professionals who decided whether to seek an examiner (if, indeed, they considered such values at all).

[146] A chi squared test shows no association between an examiner motion and missing asset values (X^2=2.0220, p=0.155) or missing liability values (X^2=1.3859, p=0.239).

	Assets scheduled	Assets not scheduled	Liabilities scheduled	Liabilities not scheduled
Examiner sought (n=87)	60	27	44	43
Examiner Appointed (with or without a motion) (n=42)	31	11	21	21

[147] p=0.00 on a Pearson's chi squared and Fischer's exact test.

pointments. The conditions that predict an examiner request are, in short, likely to be necessary—but not necessarily sufficient—to predict an examiner's appointment.

3.2 Economic Determinants of Examiner Requests and Appointments

The descriptive and interview data indicate that the decision to seek or appoint an examiner turns in part on the answer to an economic question: how will the costs of an examiner compare to the benefits? This part describes univariate analysis of certain relevant economic data.

3.2.1 *Debtor Size*

The average case in which an examiner was sought was almost twice as large as the sample (using median scheduled values) and more than four times as large (using mean asset values). Companies for which an examiner was sought by motion had scheduled median (mean) assets of about $750 million ($5.6 billion) (n=60), as compared to $489 million ($1.3 billion) in assets for cases in which no such motion was made (n=258) and $512 million ($2.03 billion) for the entire sample (n=358). The difference was statistically significant.[148] Similarly, cases in which an examiner was sought had median (mean) liabilities of $974 million ($4.85 billion) (n=44), as compared to $534 million ($1.55) (n=214) for companies in which no such motion was made and $557 million ($2.12 billion) for the entire sample (n=258). This, too, was statistically significant.[149] Cases in which an examiner was sought had median (mean) net scheduled assets of $79 million ($2.16 billion) (n=43), as distinct from $500 (-$348) thousand for cases in which no motion was made and $13 ($364) million for the entire sample. This, too, was statistically significant.[150]

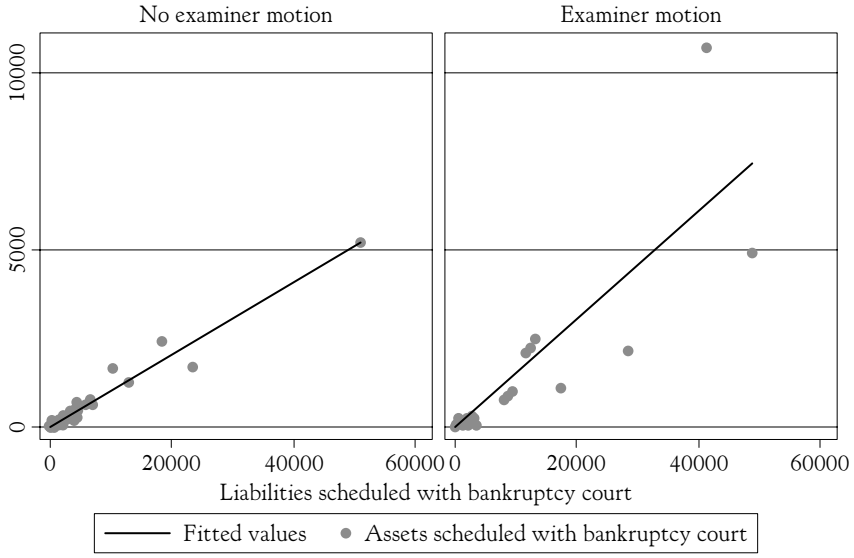
Assets and liabilities did not, however, show any statistically significant association with the grant of examiner motions. Cases in which an examiner motion was granted were actually smaller by median assets than cases where the motion was not granted; they were, however, larger by mean and net assets. Companies in which an examiner was appointed on motion had median (mean) scheduled assets of $649 million ($8.65 billion) (n=28) as compared to $780 million ($3.02 billion) (n=32) for cases where the motion was not granted. Cases in which an examiner motion was granted had median (mean) liabilities of $1.08 billion ($6.7 billion) (n=21), as compared to $775 million ($3.15 billion) (n=23) for cases in which the motion was not granted. Cases in which an examiner motion was granted had median (mean) net as-

[148]As noted above the non-normal distribution of these values suggests that a Wilcoxon rank-sum test is appropriate. This shows a statistically significant correlation, p=0.0241.

[149]Rank-sum, p=0.023.

[150]Rank-sum, p=0.002.

Figure 3.2-A Debtor Size (Examiner Motions) ($ millions)



sets of $76 million ($4.8 billion) (n=20) as compared to net assets of $95 million (-$163 million) in cases where the motion was not granted (n=23). In no case were these differences statistically significant.[151]

Consistent with the rough link between size and district, cases filed in "big" districts—Delaware or the Southern District of New York—were more likely to see requests for examiners. Of all requests for examiners, forty-six of the eighty-seven requests for examiners (52.9%) were from a big district (Delaware or the SDNY). This was not, however, a statistically significant difference.[152] Interestingly, being *outside* a big district did increase the chance that an examiner would be appointed, although whether the increase is statistically significant turns on whether the examiner was appointed on motion or not. Courts in big districts granted only seventeen (or 40% of) requests for an examiner as compared to twenty-two (or 56%) in other districts, although these differences were not statistically significant.[153] However, if we include the three cases where an examiner was appointed *sua sponte*, the difference between big and small districts does become statistically significant.[154] Either way, it would appear that an examiner is more

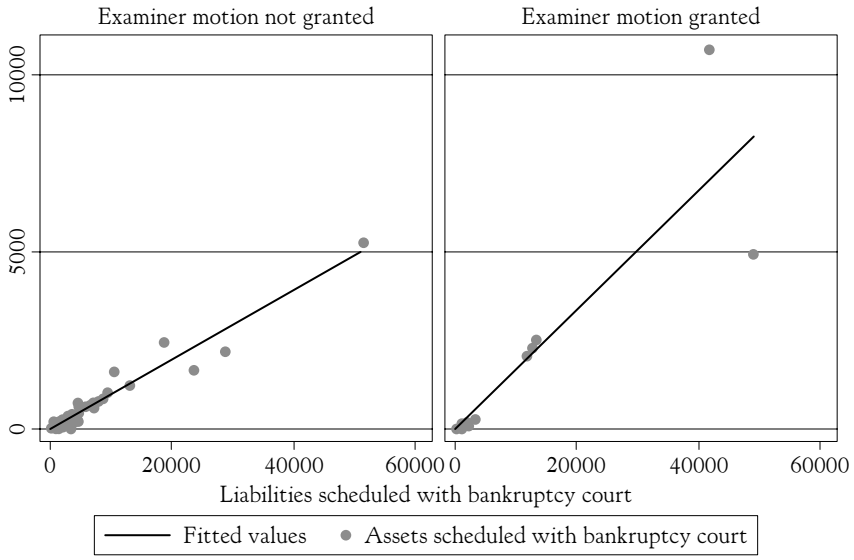
[151]In the case of assets, rank-sum p = .81; in the case of liabilities, rank-sum p = .75; in the case of net assets, rank-sum p=0.9.

[152]A Pearson's chi-squared test indicates that this difference was not statistically significant, X^2=0.3815, p=0.537.

[153]This was not statistically significant, X^2=2.4451, p=0.118.

[154]This is statistically significant on a chi-squared test: (X^2=4.3735, p=037.) and a Fisher's exact p =0.052.

Figure 3.2-B Debtor Size (Examiner Motion Grants) ($ millions)



likely to be appointed if sought in a district outside of Delaware or the Southern District of New York.

3.2.2 *Economic Outcomes—Estate Recoveries*

For forty-two of the cases in which an examiner was requested, I analyzed whether an examiner, if appointed, appeared from the pleadings likely to improve economic outcomes by, for example, increasing estate recoveries. The analysis indicates that the apparent likelihood of a better economic result did not significantly associate with an examiner being either requested or appointed.

Determining whether an examiner would likely improve estate recoveries required judgment calls. Clear examples would be where an examiner investigates allegations that a debtor engaged in a prepetition fraudulent transfer or that directors and officers had breached fiduciary duties to the debtor. These are allegations which, if true, would result in litigation or settlement that brings money into the estate. Other, less certain examples of potentially better outcomes were cases where an examiner was sought to investigate intercompany claims or questions of substantive consolidation. The results of these examinations might improve the movant's economic outcome by reducing other (dilutive) claims (but, of course, might not).

In other cases, however, there was no apparent economic benefit from having an examiner. In some cases, for example, an examiner was sought to investigate securities fraud claims which, if successful, would most likely result in direct claims of securities holders against the defendant (and not bene-

fit the estate). In other cases, an examiner may have been sought to investigate questions about accounting practices or to resolve conflicts that would have no apparent affect on distributions in the case. Cases were coded as not likely to affect economic outcomes only if no element of the request (if approved) appeared likely to do so.

Examples of both types of cases, and explanations for their treatment, are discussed further in Part 4 below, and are set forth on Table 3.2.2 (attached). An estate recovery would have been a likely result of appointment of an examiner in about half of those cases (twenty-two or 52.4%). Of the twenty-five of these cases in which an examiner was appointed, 60% were likely to result in an estate recovery (n=15), while 40% were not (n=10). This was not a statistically significant association.[155]

3.3 Contextual Determinants of Examiner Requests and Appointments

Economics appear to have some bearing on requests for examiners, although not their appointment. Other factors that might matter include certain qualities of the cases—allegations of fraud, complexity, contentiousness—observed indirectly through the data. Here, too, I find that while there is some association between these contextual factors and examiner requests, these factors do not (in most cases) associate with actual appointments.

As with size, fraud appears to matter for examiner requests but not appointments. Thirty-one cases in the Examiners Database (5.4%) coded for allegations of fraud. Although an examiner was only requested in nine of those thirty-one fraud cases, this is statistically significant on both a Pearson's chi squared[156] and Fisher's exact test.[157] Yet, allegations of fraud had little bearing on whether an examiner was actually appointed. These same tests show no statistically significant association between the presence of fraud and the appointment of an examiner, although (again) sample size limited the strength of inference.[158]

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[155]Pearson's X^2=1.437, p=0.23.

[156]X^2=4.9566, $p<0.05$.

[157]Fisher's exact=0.037. The following cross-tabulation shows the number (and percentage) of cases involving fraud and examiner requests.

	No Examiner requested	Examiner requested	Examiner not appointed	Examiner appointed
Case did not involve fraud	467 (95.5%)	78 (89.66%)	44 (91.67%)	34 (87.18%)
Case involved fraud	22 (4.5%)	9 (10.34%)	4 (8.33%)	5 (12.82%)
Totals	489 (100%)	87 (100%)	48 (100%)	39 (100%)

[158]X^2=0.4671 (p=0.494); Fisher's exact=0.507.

I note, however, that even though there is a correlation between fraud and examiner motions, examiners were rarely sought (and thus rarely appointed) in fraud cases. They were requested in fewer than one-third of cases involving fraud (nine of thirty-one cases), and appointed in two-thirds of those (five of nine cases).[159] Given the statutory criteria, Congress' goals in creating the examiner, and the nature of these cases—large, public companies with credible allegations of fraud—it remains striking that there were not more requests and therefore grants. These are the paradigm cases for examiners, and yet they produce less than paradigmatic results.

The dockets for cases in the Examiners Database indicate that two other non-economic factors show a statistical relationship with such requests: case complexity and case contentiousness.[160]

3.3.1 *Complexity*

If the role of the examiner was created to address informational problems—to tell the story of failure—we might expect to see them more frequently in cases that are considered more "complex." This is indeed the case. Complexity, understood in certain ways, is associated with both requests for examiners and their appointment.

Complexity could refer to many different things. I analyzed complexity from two perspectives: that of the company and that of the case itself. To determine whether a company was complex, I analyzed, among other things, the number of entities in the debtor group, the aggregate number of employees, and the number of jurisdictions in which entities in the debtor group were formed.

These measures of company complexity were not associated with requests for or appointments of an examiner. To determine whether the number of entities in the debtor group was associated with examiner requests or appointments, I conducted the analysis two ways: first, including all companies and, second, after excluding the three largest companies.[161] Both analyses indicated that there was not a statistically significant association between this measure of company complexity and examiner requests. The only factor

[159]In no fraud case was a trustee appointed instead of an examiner; indeed, trustees were appointed in only two fraud cases.

[160]I acknowledge that dockets are only indirect evidence of complexity or contentiousness. Local legal cultures may produce variations in practice that, in turn, result in greater or lesser numbers of filings, and thus larger (or smaller) dockets. Attorneys may make oral motions that are denied but never reflected in the dockets.

[161]I conducted the second analysis without the three largest companies because the atypical complexity of these companies could have been masking an association between complexity and examiner requests in the rest of the sample. The three most complex companies (as measured by the number of debtors) were *Loewen Group* (1098 debtors); *Integrated Health Services* (662 debtors); and *Genesis Health Services* (416 debtors). Given that the average number of debtors was 41, these three companies had more than ten times as many debtors as the average company.

about a debtor group that appeared to matter was whether the debtor had at least one subsidiary formed outside the United States. Examiners were sought almost twice as often (23.6% to 13.9%) for companies with at least one overseas subsidiary as compared to those with none.[162] This may be coincidence, or it may be consistent with the observation of one subject interviewed for this project who indicated a belief that, as in the *Maxwell* bankruptcy, examiners could play an important role in transnational chapter 11 cases.[163]

In contrast to company complexity, case complexity did have a statistically significant relationship to examiner requests. Case complexity was measured by, among other things, case duration and the number of docket entries. Cases with requests for examiners had a mean (median) duration of 593 (480) days (n=82)[164] in bankruptcy, as distinct from cases without, which had a mean (median) duration of 456 (361) days (n=445), a statistically significant association.[165] Cases in which an examiner was sought and appointed had a mean (median) duration of 657 (635) days (n=36).[166] Cases where an examiner was sought but not appointed lasted a mean (median) of 543 (351) days (n=46).

The number of docket entries was an even stronger indicator of the presence of a request for or the appointment of an examiner. Cases in which an examiner was sought had on average (median) 4337 (2805) docket entries (n=85), whereas cases without such a request had on average (median) 2280 (1485.5) docket entries (n=466).[167] The number of docket entries is also associated with the grant of requests for an examiner. Cases in which an examiner was sought and appointed had a mean (median) of 5,738 (3435) entries (n=37), whereas cases in which an examiner was sought but not appointed had a mean (median) of 3257 (2593) docket entries (n=48). This, too, was statistically significant.[168]

3.3.2 *Contentiousness*

Chapter 11 reorganization is premised in large part on the belief that a debtor's stakeholders would rather switch than fight. It is thus expected to be a negotiated process. But reorganization is not immune from debilitating disputes. When the disputes are severe enough, a court may appoint a trus-

[162] $p<0.05$.

[163] *See* Interview with E-2 dated Feb. 19, 2008.

[164] The number of observations in this paragraph and the next are not necessarily consistent with the observations in Table 2.3.2 because I do not have values for the number of days or dockets for all cases in the Examiners Database.

[165] A rank sum test shows this to be statistically significant at $p< 0.000$.

[166] A rank sum test shows this to be statistically significant at $p= 0.049$.

[167] Rank-sum test: p=0.00.

[168] Rank-sum test: p=0.05.

tee to replace management.[169] Sometimes, however, disputes are severe enough to warrant judicial intercession but not so severe as to warrant the costs of a trustee. In those cases, a chapter 11 examiner may be used.

A number of system participants interviewed for this project indicated that they believed examiners would be appointed as a "fallback" measure in response to a request for the appointment of a trustee or conversion or dismissal of the case. Several indicated that the examiner in *Refco,* for example, was appointed as a less severe remedy than a trustee. *Refco* was a complex and potentially volatile case, involving a large number of broker dealers and allegations of massive fraud by management. One participant who was heavily involved in the case explained that an examiner was sought rather than a trustee, because "filing a trustee motion, and the appointment of a trustee, is one of the . . . catastrophic remedies that the bankruptcy court can impart on a chapter 11 debtor."[170] Despite pressure from the Justice Department to appoint a trustee in *Refco*, an examiner was considered preferable, at least in the short term, because if a trustee were sought (or appointed) "the brokers would flee," thereby reducing value for creditors.[171]

Similarly, some participants noted that examiners might be appointed when it appeared there was a breakdown in the expected negotiating dynamic. In the *FiberMark* bankruptcy, for example, Silver Point L.P., a hedge fund that traded in distressed debt, was invited to join the official creditor's committee after it acquired a large position in FiberMark's public notes. The committee was, according to the report of examiner Harvey R. Miller, dominated by another creditor, AIG Global Investment Corp., and its workout specialist, Thomas Musante. Conflicts between Silver Point and AIG resulted in significant and costly disruptions, including allegations (unsubstantiated) that Silver Point engaged in illegal trading in FiberMark claims. According to Miller, committee members "resort[ed] to strategic litigation based upon doubtful claims . . . [which] further inflamed an already counterproductive environment to the detriment and prejudice of the reorganization process and the interest of creditors other than AIG . . . and Silver Point." The examiner explained that, from the commencement of the case—

> a state of war existed among FiberMark and its professional advisors . . . on one side, and Mr. Thomas A. Musante, a

[169]In *In re Marvel Entn't Group, Inc.,* the Third Circuit Court of Appeals held that cause to appoint a trustee exists where "inherent conflicts extend beyond the healthy conflicts that exist between debtor and creditor, or . . . , when the parties 'begin working at cross-purposes.'" 140 F.3d 463, 472-73 (3d Cir. 1998) (quoting *In re* Cajun Elec. Power Coop., Inc., 74 F.3d 599, 600 (5th Cir. 1996)).

[170]Interview with O-1 dated Sept. 27, 2007.

[171]*Id.* Similarly, an interview subject who had been the examiner for a large debtor indicated that he believed he was appointed as an examiner rather than a trustee because a trustee would "destabilize" the company's business. Interview with E-2 dated Feb. 19, 2008.

> "work out" specialist and employee of AIG Global Investment Corp on the other side. On the Commencement Date, AIG was a holder of approximately $65 million or approximately 19% of principal amount of FiberMark's public notes. The commencement of the chapter 11 cases literally incensed Mr. Musante and his need to discipline FiberMark and its professionals thereafter permeated the administration of the chapter 11 cases. As a result, what appeared to be a simple, uncomplicated reorganization case with the primary goals of substantially reducing FiberMark's debt obligations and expeditiously emerging from chapter 11, soon evolved into a clash of personalities and philosophies.[172]

The *FiberMark* examiner estimated that the delay caused by these fights reduced the value of distributions to creditors by almost $60 million.

Yet, allegations of conflict do not automatically result in the appointment of an examiner. In the *Loew's Cineplex* case, for example, one creditor, Merrill Lynch, opened its memorandum of law in support of its examiner motion thus: "The creditors' committee process has failed in these cases."[173] A second creditor, Six West, also sought appointment of an examiner, due apparently to claims arising from prepetition litigation with the debtor.[174] Although the Merrill Lynch motion was settled and withdrawn (for reasons not explained in the record), the debtor objected to the Six West motion, arguing that it was "a transparent effort to gain an unfair advantage in the litigation between the Debtors and [movants] that has been pending since 1997."[175] This second motion was, according to the debtors, the "paradigm of an unreasonable and vexatious pleading."[176] For reasons not reflected in the record, no examiner was appointed.

Like "complexity," "contentiousness" is a composite impression. One way to measure the contentiousness of a case is by the number of requests to

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[172]Report of Harvey R. Miller, as Examiner, at 2, *In re* FiberMark, Inc., No. 04-10463 (Bankr. D. Vt., Aug. 16, 2005) (Docket No. 1805).

[173]Memorandum of Law in Support of Motion of Merrill Lynch, Pierce, Fenner & Smith, Inc. for Entry of an Order Directing the Appointment of an Examiner, and for Filing of Memorandum of Law Under Seal, together with Notice of Filing of Redacted Memorandum of Law attached thereto, at 1, *In re* Loew's Cineplex Entm't Corp., No. 01-40346 (Bankr. S.D.N.Y., Nov. 21, 2001) (Docket No. 913).

[174]*See* Redacted Cross-Motion of Six West Retail Acquisition, Inc. for Appointment of an Examiner and Memorandum of Law in Support of Same filed by Jeffrey L. Schwartz on behalf of Six West Retail Acquisition, Inc., *In re* Loew's Cineplex Entm't Corp., No. 01-40346 (Bankr. S.D.N.Y., Feb. 22, 2002) (Docket No. 1180).

[175]*See* Response of Debtors and Debtors-In-Possession to Objection of Six West Retail Acquisition, Inc. To Debtors' First Amended Chapter 11 Plan and Redacted Cross-Motion of Six West Retail Acquisition, Inc. for Appointment of An Examiner, at 2, *In re* Loew's Cineplex Entm't Corp., No. 01-40346 (Bankr. S.D.N.Y., Feb. 27, 2002) (Docket No. 1192).

[176]*Id.*

appoint a chapter 11 trustee or to convert or dismiss the case. These motions may be evidence of a serious breakdown in the negotiating process that Congress envisioned in the chapter 11 structure. These motions may be made for strategic reasons—because the movant wants to threaten intransigent management—or because the movant genuinely believes the reorganization process has failed. Either way, such requests suggest a case that is far more contentious than is ordinary.

The data indicate an association between requests to appoint an examiner and motions to appoint a chapter 11 trustee or to convert or dismiss the case. Trustees were requested in eighty-one cases (14.1%); examiners were requested in eighty-seven cases (15.1%). In twenty-eight cases, both a trustee and an examiner were sought, indicating a strong statistical correlation.[177] Yet, as with other data that would seem related to examiner requests and appointments, there is no strong association between trustee requests and examiner appointments. In ten of the cases where both were sought (35.7%), an examiner was actually appointed. While examiners were more than twice as likely to be appointed if there had also been a trustee motion (35.7% v. 12.9%), this was nevertheless not a statistically significant relationship in isolation.[178] Trustees were actually appointed in far fewer cases (twenty-four, or 4.2%) than examiners (forty-two, or 7.39%, including three *sua sponte* appointments).[179]

Motions to convert or dismiss a case also correlated strongly to requests for examiners, but not with their appointment. A motion to convert or dismiss a case (or a portion thereof) was filed in 147 cases (25.5%). Both an examiner and conversion or dismissal were sought in 29 cases. It was more likely that an examiner would be sought in a case in which a conversion or dismissal had also been requested.[180] Yet, as above, there appears to be no statistically significant relationship between conversion/dismissal motions and examiner appointments. Of the twenty-nine cases in which both motions were filed, an examiner was appointed in eleven, and not appointed in eighteen.[181]

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[177] $X^2=27.8466$, $p<0.001$

[178] $X^2=1.3865$, $p=0.239$.

[179] In two cases, (*Baldwin Builders* and *Enron*) both an examiner and a trustee were appointed. An examiner and a trustee could be appointed in the same case if the examiner were appointed first or if a trustee was appointed for one entity in the debtor group and an examiner for another. The same would be true for conversion or dismissal.

[180] $X^2=3.2905$, $p<0.07$.

[181] Motions to convert or dismiss a case were granted in 60 cases, or about 10% of the sample. As noted above, in about seventeen cases, the conversion/dismissal motion was granted notwithstanding the confirmation of a plan. This may indicate less contentiousness than the raw number of conversion/dismissal motions would suggest. In these cases, it appears, cases were dismissed for debtors not part of the confirmed plan.

While the relationship between examiner requests, on the one hand, and requests for a trustee or conversion/dismissal, on the other, might indicate that examiner cases are more contentious than average, there is some reason to believe they are still less contentious than cases where a trustee or conversion/dismissal is sought. This is due in part to the correlation between cases with examiner requests and the outcome of the plan confirmation process. In general, the confirmation of a plan is likely to indicate that major disputes were probably resolved.

The data indicate that while examiner cases are more volatile than the norm (by docket entry and requests for related relief), these cases are still less contentious than cases where a party sought a chapter 11 trustee or conversion or dismissal. This is because cases in which examiners were sought were more likely to result in confirmed reorganization plans than were cases where a party moved for a trustee or conversion or dismissal. Of 489 cases with confirmed plans, examiners were sought in seventy-nine; examiners were sought in only two of the forty-five cases in which a plan was not confirmed. Examiner requests show a statistically significant correlation with confirmation.[182] If we consider plan confirmation to be evidence that disputes were mostly settled, then examiners may be seen as appearing more frequently in cases that are less contentious than those involving requests for trustees or conversion or dismissal. Interestingly, the relationship is even stronger between the filing of a prepackaged plan and the request for an examiner.[183] As with other factors, plan confirmation (or the use of a prepackaged plan) shows no correlation to the appointment of examiners.[184]

3.4 Regression Analysis

Several variables in the univariate analysis were associated with examiner requests. How do they interact in a multivariable model? I used the significant variables discussed above to build a logistic regression model. The final model demonstrates that the odds of an examiner motion were 5.75 times greater in a large case (meaning one with at least $100 million positive net assets) than in a case with negative net assets and no trustee motion. Transforming odds ratios to estimated probabilities through conditional standardization of the sample shows that a smaller case (one that has positive net assets under $100 million) will have an 8.5% chance of having an examiner appointed if no trustee motion is also made. Adding a trustee motion to such a case increases the chances of seeing an examiner motion to about 35%.

Applying conditional standardization to the other regression coefficients

[182] $X^2=4.392$, $p<0.036$.

[183] $X^2=4.958$, $p=0.026$.

[184] Plan confirmation and appointment are not statistically significantly related ($X^2=1.64$, $p=0.2$), nor are prepackaged plans and appointments ($X^2=0.43$, $p=0.5$).

in the model allows estimated probabilities for examiner motions across all the factors. Continuing in that vein, a large case (net assets in excess of $100 million) having no trustee motion has a 23% chance of an examiner motion. The greatest likelihood of having an examiner motion—a 63% chance—occurs in large cases (net assets in excess of $100 million) where a trustee motion is also made. Table 3.3 (attached) summarizes the odds ratios, significance, and confidence intervals for the regression model.

As with the univariate analysis discussed above, sample size was insufficient to test which factors were associated with granting an examiner motion. Even factors such as case duration and docket length lacked statistical power to show the extent to which they, in concert with the other variables, influenced the success of motions to appoint examiners. This is due to the small number of observations of the dependent variable, examiner appointments.

As noted above, the foregoing variables were modeled in a logistic regression. With one problematic exception, none was statistically significant. The exception regressed examiner appointments against net assets and cases in small districts (that is, outside of Delaware or the Southern District of New York (n=22)). On this analysis, it appears that, holding net assets equal, the odds of having an examiner appointed in a small district is greater than in a big district; this was statistically significant.[185]

This is a provocative finding, given the heated debate over the effect that venue choice has on reorganization.[186] It would be exciting to make a strong claim about the effect that venue has on examiner appointments. The reality, however, is that there are only two positive-net-asset cases in small districts (*Mirant* and *NewPower Holdings*) in which an examiner was actually sought and appointed. So, while it is clear that, on a pure percentage basis, examiners are appointed more often in small districts than in large (as discussed above), that difference is not statistically significant; the combination of variables is not a valid predictor that an examiner motion will succeed.[187]

4. WHO ARE EXAMINERS AND WHAT DO THEY DO?

The Bankruptcy Code says nothing about the qualifications to be an examiner. Although the available pleadings did not indicate the professional backgrounds of examiners in many cases, a review of the names of the examiners appointed indicates that many (perhaps most) were attorneys. The pleadings I have obtained indicated nine were attorneys, although a review of the

[185] X^2=4.9579, p=0.03.

[186] *See generally* LoPucki, Courting Failure, *supra* note 23. R

[187] The following table shows that, while examiner appointments in "small" districts are statistically significant (*), the high confidence interval (**) indicates that this is not a valid indicator of examiner appointments.

list of names of examiners (see Table 2.2.2) suggests more than that. Some were also forensic accountants.

The process for choosing an examiner appears to be left to the office of the United States Trustee. Interviews with system participants indicate that the UST in large cases will consult with major parties in a case about proposed candidates for the position and determine whether there are any conflicts of interest or potential problems with an individual candidate. Although some system participants indicated concerns about the costs of examiners generally, they indicated that, with few exceptions, examiners in large cases were neutral, professional and competent.[188]

The Bankruptcy Code gives mixed signals on what examiners are supposed to do. On the one hand, the name "examiner" and the fact that the examiner is statutorily expected to produce a "report" suggests that their function will be informational. They are supposed to expose and explain things that others cannot or will not in ways the system deems reliable and efficient. On the other hand, Bankruptcy Code § 1106 expressly provides that examiners may do anything that a court orders the debtor in possession not to do. So, in a somewhat backwards way, the Bankruptcy Code actually contemplates the possibility that examiners will do much more than examine.

In fact, examiners do occasionally perform non-investigative functions, although the evidence suggests that this will be rare, and system participants are generally wary that these "expanded" functions might interfere with the ordinary workings of the reorganization process. As discussed above, examiners may be appointed to address concerns about the reorganization plan[189] or breakdowns in negotiations.[190] Examiners have also analyzed valuation,[191]

Examiner appointments on motion	Odds Ratio	Std. Err.	P>|z|	95% Conf. Interval
Net scheduled assets between $0 and $100 million	.4555218	.4741164	0.450	.0592327, 3.503136
Net scheduled assets above $100 million	1.619551	1.341031	0.560	.3195785, 8.207521
"Small" district (not SDNY or DE)	8.208248	7.555269	0.022*	1.351336, 49.85831**

Adding the three sua sponte appointments (all from small districts) does not change the result. It produces no statistically valid effect in the model.

[188]This is not always the case. In *In re Big Rivers Electric Corporation,* a case not in the Examiners Database, the court ordered disgorgement of fees paid to an examiner who had negotiated a "success fee" with certain unsecured creditors, thus impugning his independence and duty of loyalty to the estate. *See In re* Big Rivers Elec. Corp., 355 F.3d 415 (6th Cir. 2004).

[189]*In re* SpectraSite Holdings, Inc. (02-03631); *In re* FLAG Telecom Holdings (02-11732).

[190]*E.g.*, *In re* UAL Corp. (02-48191) (labor dispute); *In re* Fibermark, Inc. (04-10463) (allegations of UCC member misconduct).

[191]*E.g.*, *In re* Loral Space & Commc'n (03-41710); *In re* Geneva Steel Co. (99-21130) (debtor's going concern viability).

the debtor's corporate structure,[192] and a regulated debtor's rate structure, among other things.[193] One attorney observed that in a large chapter 11 case involving a manufacturing company, the examiner functioned as an "ombudsman," trying to manage disputes among the parties.[194] Another system participant (who had been, at various points an examiner and a bankruptcy judge) indicated that, as an examiner, he had effectively functioned as the chief executive officer of a debtor.[195]

An examiner's most controversial non-investigative role would be as a litigant on behalf of the estate. As noted above, the SABRE Report has proposed that the Bankruptcy Code be amended specifically to give examiners the power to sue on behalf of the estate. While examiners have been given this power, those interviewed for this project generally objected strongly to giving it to them. One attorney stated that he "strongly disagreed" with the SABRE proposal. "When I think about what the SABRE really wants," this attorney stated, "it's to have someone who will get behind the positions of the parties so the judge knows who to listen to. But bankruptcy is partly an adversary system."[196] Those with an interest in the outcome should litigate the dispute.

Several observed that giving examiners the power to sue would interfere with the independence and objectivity examiners are expected to bring to their investigations. "The whole purpose of the examiner," one said, "is that they are objective. And if you appoint an examiner who then can be compensated for prosecuting, you've lost that objectivity"[197] As one former member of the United States Trustee's office put it: "We have an examiner who can sue: He's called a trustee."[198]

Another, somewhat more subtle, role for examiners will see them filling power vacuums in one way or another. A number of system participants observed that they believed this was the reason two examiners were appointed in the *Enron* case. Certain Enron subsidiaries, in particular Enron North America (ENA), did not have their own creditors' committees, yet their creditors were likely to be affected by the aggregate proceedings. Enron Corp., the parent, did have a creditor's committee, but its creditors were, in some cases, potential targets of claims by the estate. Moreover, given the structure of the entities, there was no reason to expect those creditors to

[192]*In re* Grand Court Lifestyles (00-32578).

[193]Indeed, several subjects interviewed for this project indicated that, especially in the context of regulated utility bankruptcies, the examiner did more than one of these things. Interview with L-3 dated Sept. 24, 2007; Interview with L-4 dated Jan. 28, 2008.

[194]Interview with L-1 dated Sept. 24, 2007.

[195]Interview with E-2 dated Feb. 19, 2008.

[196]Interview with L-3 dated Sept. 24, 2007.

[197]Interview with J-2 dated Oct. 10, 2007.

[198]Interview with O-1 dated Sept. 27, 2007.

represent adequately the interests of creditors of ENA. Yet, appointing a separate committee to represent the creditors of ENA was considered costly and could potentially create greater conflict. An examiner for ENA would, according to those interviewed, be a more efficient way to identify and represent the interests of those creditors.[199]

Indeed, examiners are said often to be "fallbacks," alternatives to other, more severe solutions to conflicts of interest, power gaps, or disruptions to what might be considered the "ordinary" dynamics of reorganization. Thus, examiners are said to be alternatives to requests for trustees[200] (and this appears to be the case) and to requests for additional committees, especially equity committees in cases where the judge may have doubts about the likelihood of any recovery for equity.

While examiners are more likely to perform an informational role in large cases, there can be variations on this theme. As noted, sometimes the investigation or examination has nothing to do with pre-bankruptcy misconduct. In *FiberMark*, for example, the examiner investigated alleged breaches of fiduciary duty and other forms of misconduct by members of the creditors' committee. In other cases, examiners have analyzed complex rate structures, performed valuations, or assessed the debtor's capital structure.

The fact that an examiner's report is presumptively public may also affect the dynamics of the case, and participants' posture toward an examiner. One bankruptcy judge suggested that this form of publicity can influence the negotiations that typically occur in reorganization. The "important dynamic" of an examiner appointment, this judge stated, is that the examiner makes a report that is usually public. "Most of the negotiations in a chapter 11 case are not made public. So, making information public can have a very substantial impact on the negotiations themselves."[201] Making this information public may or may not be helpful in any given case. "If the examiner finds evidence of conduct that is . . . improper but can be rectified and should be taken into account in the plan but doesn't need to be published in the newspaper, that could be found by other parties and used for negotiating a plan."[202] Publicly disclosing this information in an examiner's report, this judge indicated, "might make it difficult or impossible to negotiate a plan" that takes advantage of this information.

Another informational function of an examiner that has little to do with

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[199]*See* Interview with J-2 dated Oct. 10, 2007 ("[A]t Enron there was one debtor that had a lot of creditors, ENA and they felt that the committee didn't represent adequately their interests . . . [the ENA examiner] was really looking out for ENA.").

[200]*See* Interview with J-5 dated July 16, 2008 (stating that in practice a party seeking an examiner would "typically file a motion for a trustee or in the alternative for an examiner").

[201]Interview with J-1 dated Sept. 28, 2007.

[202]*Id.*

investigating prebankruptcy misconduct involves foreign proceedings with a U.S. component. One system participant indicated that he believed that examiners would become more common as bankruptcy becomes increasingly international. This is because examiners would be in a unique position to communicate with foreign courts or insolvency authorities about the U.S. portion of the process. The examiner would have an official status distinct from management that would "allow the examiner to communicate comfortably with foreign representatives and with the foreign courts and vice versa."[203] The relatively unusual nature of U.S. reorganization—which presumptively leaves the debtor's management in possession and control of the company—may require explanation to these foreign entities, where the company may be taken over by a liquidator or conservator.[204] An examiner could overcome these barriers. Participants interviewed for this project point to the appointment of an examiner for this purpose in the infamous *Maxwell* bankruptcy, which followed the death of the media magnate Robert Maxwell.[205] The recent introduction of Chapter 15 to the Bankruptcy Code—which sets forth rules on the recognition of foreign insolvency proceedings—might increase the number of international insolvencies that take place, in part, in U.S. bankruptcy courts and, thus, in the utility of an examiner.

5. WHY AREN'T EXAMINERS MORE COMMON?

Although examiners are much more likely to appear in larger cases, or those that are more complex or contentious, the fact remains that they are rare, even in the largest cases. While we cannot know with certainty why system participants do not seek examiners more often in large cases, having some insight into this question would help explain when examiners will be sought and appointed and the work that they can do.

Interviews with system participants suggest three hypotheses about the infrequency of examiners: (1) professionals—in particular lawyers for UCCs—will resist examiner appointments as interfering with their work; (2) examiners will only rarely be expected to produce net positive recoveries to the estate, suggesting that on a cost-benefit basis, system participants do not view them as worthwhile features of most cases; and (3) the statutory framework that creates examiners inadvertently renders the work they are likely to do of little, if any, real benefit to the investing public, because the information they produce will tend to benefit estate creditors generally, not public investors specifically.

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[203]Interview with E-2 dated Feb. 19, 2008.

[204]*Id.* ("[M]ost of the world can't image a debtor in possession. It's just not part of the insolvency law of most of the world. And so with the debtor in possession, the question is, how will the foreign court know that there is an official person to deal with?").

[205]*Id. See In re* Maxwell Commc'n Corp., No. 91 B 15741 (Bankr. S.D.N.Y. Aug. 5, 1994).

5.1 Professional Turf Protection

The claim that professionals might impede requests for and appointments of examiners is alluring. As several participants interviewed for this study acknowledged, professionals might view the appointment of an examiner as a threat to their fees,[206] their influence over the case, or both. Others observed that those who represent the more common players—creditors' committees, for example—will believe that they have a duty to do the sort of an investigation that an examiner might undertake.[207] If an examiner is appointed, the examiner would presumably do something—an investigation, for example—that the creditors' committee's counsel would not. It might also interfere with management's (and DIP counsel's) efforts to reorganize the debtor. This would also be consistent with claims that large bankruptcy cases are heavily influenced by—and benefit—a small number of large law firms and bankruptcy professionals (e.g., turnaround experts).[208]

The reality, however, is a bit more complex. First, as noted above, the party most likely to seek an examiner is an individual (non-bondholder) creditor, who made thirty-two requests (36.7% of all examiner requests). Nor are creditors' committees shy about seeking examiners. They requested examiners in fifteen cases, which would seem to be more than sheer self-interest would counsel. True, a UCC was also the second most likely party to object to an examiner request (objecting in twenty-four cases, or 40% of cases in which an objection was filed), but, as noted above, no opposition was filed at all in twenty-five cases (or a little less than half of all cases involving examiner requests).

Second, professional self-interest may be couched in terms of minimizing costs in general. System participants frequently observed that judges were very concerned about the costs associated with an examiner.[209] Several par-

[206]"My god," said one attorney (sarcastically) who frequently represents equity holders in large chapter 11 cases, "is that really an issue? I think that's unfortunately the case in some cases." Interview with L-2 dated Oct. 5, 2007. A judge had the following observation: "I would phrase the concern this way: One of the concerns of professionals is getting paid and examiners tend to be expensive and one of the things that they worry about is if an examiner is appointed that means that everybody will get less reimbursement. It might be less work but it might also be as much work but just less money." Interview with J-1 dated Sept. 28, 2007.

[207]Interview with L-1 dated Sept. 20, 2007 (what "militates most against examiner and trustee appointments is the desire of creditors to conduct an investigation for themselves. That is invariably the position of creditors. They would argue that it's their duty."). One subject interviewed for this study, who had been an examiner in a large chapter 11 case, observed that an examiner "may dilute the power of the creditors' committee. Creditors' committees in recent years have wanted to conduct their own investigations." Interview with E-2 dated Feb. 19, 2008.

[208]LoPucki, Courting Failure, *supra* note 23. R

[209]As one judge explained—

> Well, the problem is, once you appoint an examiner, typically, the examiner is simply turned loose. With no budget, no restraints on how much he or she spends.

ticipants recounted anecdotes about judges who, doubtful about the merits of an examiner, but mindful of the "mandatory" nature of the statute, responded to examiner requests by saying, in substance, that they would appoint an examiner "but give him nothing to do and no budget."[210]

More realistically, many system participants noted that judges would often appoint an examiner with a limited budget, with the understanding that if the examiner needed to expand his or her investigation, the judge would entertain the request at that time.[211] The quid pro quo, however, would be that the examiner would have to demonstrate some basis for seeking to expand his or her mandate.[212]

Third, and perhaps most interesting, is the absence of examiner requests by public investors—or their professionals. Not only are they unlikely to request an examiner, but when they do so, it will often be on a pro se basis.[213] No filed request for an examiner came from a law firm that typically represents securities fraud plaintiffs, e.g., Milberg Weiss. If examiners were thought likely to produce information helpful to the investing public, we might expect their lawyers to seek them. In fact, they do not.

> Sometimes, with some directions as to what should be done. After that experience, what I have done since then, in the one or two times I think when I've appointed examiners, is to also give them budgets.

See Interview with J-1 dated Sept. 28, 2007. *See also* Interview with J-2 dated July 16, 2008 (observing that those who request examiners do not care about cost, but judges who appoint them do.).

[210]Interview with L-4 dated Jan. 28, 2008 (paraphrasing a judge from the Southern District of New York in response to a request for an examiner, as follows: "You want an examiner for a day? Under *Revco* I can define the scope narrowly.").

[211]A judge in one recent, prominent large case explained as follows:

> I limited the scope of the examination to things that had not really been focused on yet by the creditors committee and also imposed a budget, and that was done as part of a budgeting process that the examiner and his counsel and various parties and interests went through first. I wasn't happy with what the examiner proposed at first, they sent it back and did it again and they finally got it right. And actually at the end of the day, I was quite pleased with the work that the examiner did and I think everyone else has been too. He came in $1,000,000 under budget and it was a tight budget, and his report I think, was quite useful in terms of the litigation that has been brought since then as part of the, you know, post chapter 11 plan litigation.

Interview with J-2 dated Oct. 2, 2007.

[212]One attorney who frequently represents large debtors was still skeptical about the costs and benefits of examiners. "You [try] to keep control," he said, "by limiting the examiner to six months and a fee cap of X. But, lo and behold, to no one's surprise, the examiner says he has found A, B and C, which he believes will lead to D, E and F, and the scope [of the examination] has to expand, and it will take X more dollars and Y more months to do so. I knew very few judges who would decline to expand the inquiry." *See* Interview with L-1 dated Sept. 20, 2007.

[213]Ten requests were on a pro se basis. Of those ten, eight were identified as individual investors.

5.2 Estate Recoveries

A second explanation for the infrequency of examiners is that they will only be sought and appointed when they are likely to produce information that leads to an economic gain for the estate, in particular unsecured creditors. The logic here would be that an examiner will only be sought or appointed if it appears *ex ante* that the investigation is likely to be cost-justified.

The cost-benefit analysis behind an examiner appointment is likely to be complex. Costs will be easy to imagine. These will most obviously include the cost of the examiner and/or his or her professionals. In some cases, these costs can be significant. The examiners in *Enron* famously cost about $100 million.[214] While system participants may have gotten over the "sticker shock" of this examination,[215] the cost of an examiner can be difficult to justify when a company has limited cash flow. This may help to explain the association observed in Part 3 between large net positive asset values and examiner requests.

Nor are these the only costs. Examiners will take the time and resources of the participants they investigate. Some participants observe that examiners can insert themselves into disputes in ways that may not be constructive, acting as "ombudsman" to address "problems" that do not concern the parties.[216]

The benefit side of the equation is likely to be much more speculative. As discussed above, an examination will generally be viewed as cost-justified

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[214] A review of the dockets from *Enron* indicates that the examiners and their professionals billed in excess of $100 million. The orders granting fees to the examiners and their professionals were entered Feb. 15, 2006 (Docket No. 28924) and Mar. 6, 2006 (Docket No. 29054), respectively. The final fee-granting order (to any professional) was entered Aug. 10, 2006 (Docket No. 30095). Although "examiner's" fees are not the subject of the final order, it does contain a summary of compensation for all professionals involved. The following figures represent [Professional Fee] + [Expenses] = [Total].

> Harrison J. Goldin and Goldin Associates, LLC: 11,627,568.75 + 1,601,621.50 = 13,229,189.50
> Neal Batson and Alston & Bird LLP:
> Neal Batson, Esq.: 1,809,810.25 + 10,325.95 = 1,820,136.20
> Alston & Bird LLP: 71,066,038.04 + 14,577,275.89 = 85,643,313.93
> Combined: 72,875,848.29 + 14,587,601.84 = 87,463,450.13
> Other Professionals Retained by Batson:
> Plante & Moran PLLC: 6,185,693.99 + 476,834.20 = 6,662,528.19
> George J. Benston, Ph.D: 420,452.50 + 1,502.00 = 421,954.50
> Al Hartgraves, Ph.D: 401,340.00 + 88.00 = 401,428.00
> Combined: 7,007,486.49 + 478,424.2 = 7,485,910.69

[215] *See* Interview with O-1 dated Sept. 27, 2007.

[216] *See* Interview with L-1 dated Sept. 20, 2007. This attorney observed that in one very large case where he represented the debtor in possession, an examiner was "in some respects helpful, in some not. As predicted, he was an additional force to contend with in negotiations. He had a vague scope. He was in everything, and acted as an ombudsman. We had to negotiate with him" as well as other major constituencies, such as creditors' committees.

if it exposes and develops information likely to lead to recoveries for the estate that exceed the cost of the examiner, plus the costs of litigating the cause of action, or because it reduces the claims base to produce a comparable economic benefit to unsecured creditors. In other cases, examiners are only rarely appointed, the story goes, because they are expected to produce no net economic benefit to the bankruptcy estate.

System participants frequently suggested that an examiner was more likely to be sought or appointed if it appeared that the examination would produce recoveries for the estate that could not be developed through the ordinary adversary process.[217] Yet, as discussed in Part 3, it would appear from a review of the pleadings that examiners are often requested for reasons that would not, realistically, benefit estate stakeholders economically.

One reason the prospect of estate recoveries may not lead to more examiner appointments has to do with the adversarial nature of the bankruptcy system. In many cases, the creditors' committee believes it can and should perform various investigations, in part because it is acting for stakeholders (unsecured creditors) who would likely benefit from the investigation. Indeed, if examination was only about avoidance actions, it would appear that an examiner's analysis would just be a (needlessly costly?) substitute for the discovery that an estate fiduciary (e.g., the creditors' committee) would engage in if it were suing or contemplating suing on behalf of the estate.[218] To the extent we believe that examiners exist only to produce reports that result in net positive estate recoveries, we set them up to fail: They will be competing with the real parties in interest (e.g., unsecured creditors) and their representatives, whose professionals understandably want to control the avoidance analysis and any litigations that may result.

Moreover, this will be true in a system where adversary proceedings generally are said to be rare and declining in number.[219] Baird and Morrison, for example, report that only about 12% of chapter 11 cases from a sample stud-

[217]In assessing the role of potential recoveries, I did not look at cases in which examiners were not sought, but only the pleadings for the cases in which an examiner was sought.

[218]Interview with L-3 dated Sept. 24, 2007 ("Bankruptcy is partly an adversary system. Either you respect the adversary system, or you don't. Until you convert to an inquisitorial system, however, the lawyers and their parties [not examiners] should be making their cases."). Creditors' committees may sue on behalf of the estate, if given the power to do so in a derivative capacity. *See* Official Comm. of Unsecured Creditors of Cybergenics Corp. v. Chinery (*In re* Cybergenics), 330 F.3d 548, 566 (3d Cir. 2003) (en banc) (holding that an official creditors' committee may have standing to sue former insiders to recover alleged fraudulent transfers). *See also* Interview with L-2 dated Oct. 5, 2007 (discussing the role that *Cybergenics* plays in creating committee capacity to sue on behalf of the estate).

[219]*See, e.g.*, Elizabeth Warren, *Vanishing Trials: The Bankruptcy Experience*, 1 J. EMPIR. L. STUD. 913 (2004); Douglas G. Baird & Edward R. Morrison, *Adversary Proceedings in Bankruptcy: A Sideshow*, 79 AM. BANKR. L.J. 951 (2005) ("Bankruptcy's adversary proceeding, while resembling the civil trial, is a small (even trivial) part of the bankruptcy process . . . .").

ied in the Northern District of Illinois had any adversary proceedings.[220] Thus, while the total incidence of adversary proceedings is about 60% across their sample of chapter 11 cases (total proceedings divided by total filings, expressed as a percentage), the number of cases in which any adversary proceeding occurs is quite small. Fewer than 1% of business filings accounted for over 50% of adversary proceedings in their sample.[221]

Baird and Morrison do not explain why adversary proceedings are rare, but one answer may be the role that bankruptcy case financing plays. For example, pre-petition or post-petition lenders may fully encumber a debtor's assets, taking as collateral avoidance actions that would otherwise be assets of the estate.[222] Alternatively, the "carveout" of unencumbered assets for payment of professional fees may not be available for use in prosecuting adversary proceedings against the lenders in question.

This hypothesis may apply to examiners. Thus, the court in one case (*In re Cone Mills Corp.*), approved a cash collateral order that made appointment of an examiner "with expanded powers" a default.[223] In another case, *aaiPharma, Inc.*, the court approved a debtor in possession financing facility that forbade the debtor from seeking appointment of an examiner.[224] Lenders in these cases—not the other parties or the bankruptcy court—thus exert what may be a dispositive influence over whether an examiner is appropriate. Since it is difficult to imagine lenders (or their lawyers) benefitting from the appointment of an examiner, such practices should chill requests for and appointments of examiners, regardless of the benefits they may bring to the debtor and its estate.

A related explanation reflects concerns that examiners may sometimes be sought for strategic reasons, even where an investigation (or other examiner function) might not benefit the estate. Lawyers admitted this in interviews. One lawyer explained that he represented the UCC of one of several debtors in a single very large case. He believed his clients were "getting screwed by the operating company [another debtor in the same case]" and so sought the examiner for strategic reasons. "We never wanted an examiner, but we

[220]Baird & Morrison, *supra* note 219, at 957. R

[221]*Id.*

[222]The Third Circuit, in *In re Cybergenics*, may have made this somewhat more difficult, as it held that a debtor's sale of all assets did not include a sale of avoidance actions. Cybergenics Corp., 226 F.3d at 237.

[223]*See* Order (FINAL) (A) Authorizing the Use of Cash Collateral and (B) Granting Adequate Protection to the Prepetition Collateral Agents Pursuant to Sections 105, 361, and 363 of the Bankruptcy Code Including Replacement Lines and Superpriority Claims, at 20-21 *In re* Cone Mills Corp., No. 03-12944, (Bankr. D. Del. Oct. 30, 2003) (Docket No. 200).

[224]See Final Order Pursuant to 11 U.S.C. §§ 105, 361, 362, 363 and 364 of the Bankruptcy Code (i) Authorizing the Debtors to Obtain Postpetition Financing and Use Cash Collateral (ii) Granting Liens, Security Interests and Superpriority Claims, and (iii) Granting Adequate Protection, *In re* aaiPharma, Inc., No. 05-11341, (Bankr. D. Del., June 2, 2005) (Docket No. 135).

needed to shake the case up."[225]

Courts like those in the *Bradlee's* case have indicated that they will not be forced by parties to appoint an examiner where it is a transparent attempt to use the seemingly mandatory language for purely strategic purposes. One judge interviewed for this project observed that courts always have control over their dockets, which includes the equitable power to deny any relief on grounds such as laches.[226] This judge observed that denying an examiner request would be appropriate where it was made "right at the end of the case when a plan is being proposed so you can throw a monkey wrench into the plan process."[227]

A review of the docket-level data suggests that courts will exercise this discretion in a variety of creative ways. It is, for example, fairly unusual for a judge explicitly to deny appointment (occurring in only seventeen cases, or about 21.5% of requests). Instead, judges may instead allow examiner requests to become moot by virtue of the occurrence of some event, such as the confirmation of a plan or appointment of a trustee.[228] In twelve cases (15%) in which an examiner was sought (but not appointed), the court took no action at all.

5.3 Examiners Do Not Help the Investing Public

Examiners do not compete only with professionals who represent estate stakeholders, such as creditors' committee counsel. An even greater, and perhaps more important, competition pits them against those Congress apparently believed would be their principal beneficiaries—public investors. If Congress wanted examiners to help protect the investing public, one would expect that common guardians of the investing public—the plaintiffs' securities fraud lawyer—would frequently seek the appointment of an examiner. After all, the examination should produce information that is valuable in the prosecution by these lawyers of securities fraud suits against the directors and officers who caused or permitted the debtor's failure, at no cost to the plaintiffs or their counsel. At minimum, the threat of an examination might induce management to settle securities fraud claims, in order to remain focused on the reorganization effort.

Yet this does not happen. As noted above, eight of ten examiner requests from individual investors were pro se. Only four examiner requests came from an equity holders committee and, so far as can be observed, none came from individual investors represented by a securities fraud plaintiffs' firm.

Why do those who represent the investing public not ask for examiners?

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[225]Interview with L-4 dated Jan. 28, 2008.

[226]Interview with J-2 dated Oct. 10, 2007.

[227]*Id.*

[228]*See supra*, text at Part 2.2.3.

It may be because they believe examiners will do their clients little good and may actually be harmful. Several participants interviewed for this project indicated that examiners would, if appointed, effectively compete with the plaintiffs for estate assets, for no obvious benefit to them. While it is true that the examiner might get access to more information earlier than would securities fraud plaintiffs, especially given the stay of discovery imposed by the PSLRA,[229] an examiner "doesn't really give us access to the underlying documents any more quickly than we would otherwise [have]," one lawyer observed.[230] Indeed, the examiner "in fact may be used as an argument against giving public shareholders access when they seek documents from the debtor. 'Well,' the debtor will say, 'we're spending a gazillion dollars on the examiner's request and she's taking care of all of this, and we can't deal with her and you.'"[231]

Another lawyer explained that in cases involving especially egregious fraud, important information will come from government investigations or traditional securities fraud suits. "Grand jury investigations and securities fraud litigations may produce information of greater value to plaintiffs than an examiner."[232] Even if a shareholder argues that the appointment may be mandatory under the statute, a judge is likely to ask "what's in it for the estate?"[233]

This highlights the structural tension between the examiner's incentives and those of the investing public. An examiner's investigation—and any claims he or she develops—are likely to be derivative, meaning they would belong to the estate. They are not likely to be direct claims by the plaintiffs against the debtor's directors and officers. "If the examiner is looking primarily at prepetition misconduct, she's looking at principally derivative claims," another attorney observed. Public investors, however–

> are not pursuing derivative claims, but direct claims on behalf of individual claimants. So we are essentially competitors with the estate in this nucleus of operative facts. If the estate has the appetite to bring the claims against former directors and officers, they end up being competitors in suits for a limited pot of funds.[234]

The problem for this group is that if the examiner's report creates only

[229]Private Securities Litigation Reform Act of 1995, Pub. L. 104-67, 109 Stat. 737 (codified as amended in scattered sections of 15 U.S.C.) ("PSLRA"). The PSLRA imposes a stay on discovery during the pendency of a motion to dismiss. 15 U.S.C. § 78u-4(b)(3)(B).

[230]Interview with L-2 dated Oct. 5, 2007.

[231]*Id.*

[232]Interview with L-4 dated Jan. 28, 2008.

[233]*Id.*

[234]*Id.*

derivative claims, they are likely to be of little economic benefit to investor plaintiffs. This is because their securities fraud rescission claims are generally subordinated to the claims of general unsecured creditors under Bankruptcy Code § 510(b).[235]

Thus, the Bankruptcy Code's distributional scheme may deter public investors from using the remedy Congress thought they would. If this is correct, then examiners actually compete with their intended beneficiaries for the two things likely to matter most: actionable information and money.

A virtue of this explanation is that it stands independent of the first two hypotheses. The investing public, and those who would represent them, are not likely concerned about whether other professionals in a large reorganization will lose work to an examiner, nor would they likely care about the net economic benefit of an examination to the estate. They are likely to be interested in generating recoveries for themselves which, given the complex interaction of bankruptcy law, securities law, and principles of standing, an examiner is unlikely to assist. An examiner may have the potential to generate information of general relevance to the investing public, but the investing public likely wants more—and less—than that. Ultimately, they just want to get paid. An examiner may not help with that and may inadvertently hurt.

6. CONCLUSION—OBSERVATIONS AND RECOMMENDATIONS

The foregoing shows that the bankruptcy system has generally ignored Congress' stated intentions regarding examiners. They are not routinely sought and appointed in "large cases having great public interest."[236] They sometimes—but rarely—investigate and report on fraud, mismanagement, or the other troubles that led to bankruptcy. They sometimes—but rarely—perform other functions in the reorganization process. They have become not a fixture of the bankruptcy system that protects the investing public but instead, in the words of one person interviewed for this project, a "high bore instrument," a piece of special equipment for unusual circumstances.[237]

The data pose a normative question: Should we use examiners more than

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[235] *Id.* ("If my constituency is disenfranchised by 510(b), then claims on behalf of my constituency won't be worth much."). Section 510(b) provides in pertinent part:

> For the purpose of distribution under this title, a claim arising from rescission of a purchase or sale of a security of the debtor or of an affiliate of the debtor, for damages arising from the purchase or sale of such a security, or for reimbursement or contribution allowed under § 502 on account of such a claim, shall be subordinated to all claims or interests that are senior to or equal the claim or interest represented by such security, except that if such security is common stock, such claim has the same priority as common stock.

[236] *See supra* note 5. R

[237] *See* Interview with E-1 dated Oct. 1, 2007.

we do? The mere fact that Congress indicated that it expected them to be common is not, of itself, reason to seek or use them more. Congress gets many things wrong, and examiners may be one of them. Thus, some—notably Judge Gerber in the *Lyondell Chemical* case—want Congress to fix the "error" created by the "mandatory" language of § 1104(c)(2): examiners should be appointed only as a function of judicial "discretion."

The answer, I think, is in the data. We should use examiners more, but under the "right" circumstances, and for the "right" reasons. The right circumstances would focus on benefits to the estate and the investing public. The right reasons would reflect a cost-benefit analysis somewhat broader than the one that courts currently appear to use, to include the larger public benefits of using examiners.

6.1 The Right Circumstances—Amending the Bankruptcy Code

The limited use of examiners suggests that there is a mismatch between what Congress apparently believed it created in the Bankruptcy Code and what system participants—lawyers and judges, in particular—actually want. Not surprisingly, some (e.g. Judge Gerber in the *Lyondell Chemical* case) would amend the Bankruptcy Code to eliminate the $5 million "mandatory" appointment element of § 1104(c)(2). The reason is obvious: The fact that it appears mandatory—and the threshold is so low—may simply inspire gamesmanship, which imposes cost, delay, and other burdens on the system.

Presumably, deleting the economic test would leave the appointment of an examiner to the discretion of the judge. Left with only § 1104(c)(1), judges would appoint examiners if "in the interests of creditors, any equity security holders, and other interests of the estate."[238] Perhaps we would also replace the word "shall" with "may," or "should," or similar language.

There are, however, at least three problems with this approach.

First, if practice as identified in this paper represents larger patterns, then there may be less gamesmanship than some fear. While some examiner requests appear strategic, it is also clear that this occurs less frequently than we might expect. If cynical system participants really believed § 1104(c)(2) was mandatory, and requesting something mandatory would provide a leg up, surely they would do it more often than in 15% of cases. Similarly, the fact that judges actually appoint examiners in less than half of the cases where requested—and impose budgets and other constraints when examiners are appointed—suggests that judges have figured out how to manage the "mandatory" problem. As noted in Part 1, even without a statutory mandate, at least some courts before 1938 believed they had the equitable discretion to

[238] 11 U.S.C. § 1104(c)(1).

appoint examiners,[239] just as they today believe they have the equitable discretion to decline an appointment, notwithstanding seemingly compulsory language. The "mandatory" $5 million feature of the statute, in short, may create less mischief than we fear.

Second, the $5 million number—while it may make little sense today—is far below even the smallest case in which an examiner was requested, *NewPower Holdings, Inc.*, which had scheduled $78 million in liabilities.[240] While gamesmanship around § 1104(c)(2) may occur in cases smaller than those appearing in the Examiners Database, there seems to be little about the $5 million amount itself that draws a party to request an examiner in larger cases.

Third, there may be benefits associated with the bright line of a dollar test (albeit not the current $5 million). It creates clarity that would otherwise be lacking. How, for example, would we know when it was appropriate to appoint a trustee rather than an examiner? The standards articulated in the statute for both overlap in important respects. Both speak in "mandatory" terms: the court "shall order the appointment" of either a trustee or an examiner for "fraud, dishonesty, or incompetence" by current management or if "in the interests of creditors, any equity security holders, and other interests of the estate."[241] How would we differentiate the "interests" of creditors that warrant an examiner rather than a trustee? On what basis would an appellate court review a bankruptcy court's decision to appoint an examiner (or, more likely, not)?

If one believed that amending the Bankruptcy Code was justified, one should consider Congress' goals in creating an examiner against actual practice as we have seen it. I am not persuaded that the case has yet been made to eliminate the word "shall," but do agree that the current economic crite-

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[239] *See supra* text accompanying note 39. R

[240] The data contain only three cases scheduling liabilities below $78 million: Liberate Technologies with $21.7 million; Allied Products Corp. with $61.4 million, and Xpedior, Inc. with $50 million. None involved a request for an examiner. *See* discussion in Part 2, *supra.*

[241] 11 U.S.C. § 1104(a) & (c). A close reading of the statute shows there are (or could be) differences in approach, if we took the statute seriously: (1) According to the statute, the trustee is to be appointed "for cause," whereas the statute uses no "cause" language for examiners; (2) it appears that a trustee shall be appointed if there really was fraud etc., whereas examiners are to be appointed merely if there are "any allegations" of such misconduct; (3) there is a slightly larger menu of misconduct that might give rise to appointing an examiner than a trustee ("misconduct, mismanagement or irregularity in the management of the affairs of the debtor"); and (4) there is a larger group of people whose misconduct would lead to an examiner ("current or former" management, as distinct from "current management" for a trustee).

In twenty-eight cases from the Examiners Database, both an examiner and a trustee were sought. System participants indicated that they viewed examiners as less intrusive fallbacks than a trustee. Almost twice as many examiners (thirty-nine on motion, forty-two total) as trustees (twenty-four) were actually appointed. Without the economic metric, courts would doubtless develop criteria by which they would make the distinction, but it would presumably take time and judicial resources to do so.

rion—$5 million in unsecured non-trade claims—makes no sense.[242] If nothing else, it does not adjust for inflation. $5 million in 1978 would be about $17 million today.[243] Moreover, it has nothing to do with those whom Congress purported to protect in creating examiners—the investing public. While $5 million in unsecured debt might once have been proxy for public debt securities, it is not today. If Congress really wants to protect the investing public, it would require an examiner in cases involving a company with publicly traded securities, in particular publicly traded debt.

One way to address Judge Gerber's concerns about gamesmanship yet still retain the clear demarcation of a dollar threshold is to change the metric and the way it is used. Rather than liabilities, § 1104(c) should link an examiner appointment to something more relevant, such as the interests of the estate and the investing public. This, in turn, could be determined by creating a presumption that an examiner would be in the interests of the estate or the reorganization process if one of three conditions were satisfied: (1) there were allegations of misconduct, as under current law; (2) the debtor had publicly traded securities and assets in excess of $100 million on an inflation-adjusted basis;[244] or (3) an examiner would otherwise facilitate the reorganization process, considering the costs and benefits of an examination. Being a presumption, it could be rebutted by evidence that there are other, better ways to address the problems that led to the request for an examiner, or that there is no problem at all. In order to prevent these motions from lingering, courts would be required to act on them within sixty days. Suggested revisions to § 1104(c) appear in Appendix 3.

This approach has several virtues. First, and most obviously, it raises the economic bar, and ties it to criteria that should matter: protecting the debtor's estate and the investing public. Second, it expands the grounds for an examiner appointment to include any meaningful basis for showing that an examiner would facilitate reorganization. Thus, there would be explicit authority to appoint examiners to mediate disputes, act as international emissa-

[242]Similarly, there is little reason to enact the recommendations of the SABRE Report, which would explicitly give examiners the power to sue. *See supra* text accompanying notes 92-100. Since creditors' committees have standing to sue in cases where management cannot or will not do so, it is difficult to imagine many cases where examiner lawsuits would benefit large estates. In the rare cases where the real parties in interest (the debtor-in-possession or the creditors' committee) fail to act on their rights, and others suffer for this failure, an examiner may be an appropriate response. As written, however, the Bankruptcy Code already permits this, and some courts do it. So, an amendment is difficult to justify. R

[243]According to the *Dollar Times* inflation calculator, $5,000,000.00 in 1978 had about the same buying power as $16,926,731.08 in 2009. Annual inflation over this period was about 4.01%. *See* Inflation Calcultor, http://www.dollartimes.com/calculators/inflation.htm (last visited Nov. 3, 2009). Section 104 provides for periodic adjustments of certain dollar amounts in consumer cases, but not in Chapter 11. 11 U.S.C. § 104.

[244]As noted below, any amendment that includes a dollar trigger should include an inflation adjustment mechanism as well.

ries, and so forth, as we have seen in practice. Third, it should make gamesmanship—to the extent it occurs—less attractive. A movant would have to show that appointment was in the interests of the estate or the public for one of the reasons set forth, and not simply compulsory because the statute used the word "shall" when a debtor happens to have certain types of unsecured debt exceeding $5 million. If, notwithstanding that showing, objectors show there are other, better ways to protect the interests of the estate or investors, then an examiner would not be appointed.[245] In the process, it would force movants to show why an examiner is appropriate and opponents to show why an examiner is not. It would ground the analysis and the decision in something more useful than the seemingly arbitrary language and economics of the current statute.

6.2 The Right Reasons—Using Examiners More

Whatever the metric, we should use examiners only if there are sound reasons for doing so. What might those be?

Examiners will be warranted in at least three types of large cases.[246]

First, there will be cases in which the conventional cost-benefit calculus shows they have net positive value: the projected recoveries to stakeholders (creditors, in particular) from appointing an examiner likely exceed the examiner's projected costs. This is not, apparently, what Congress thought was supposed to happen—the statute says nothing about a cost-benefit analysis—but that appears to be what occurs in many cases anyway.

Cases where the benefits of an examiner clearly outweigh the costs to the parties would be rare. These may, for example, be cases that require a neutral assessment of the viability of potential avoidance or similar actions because it would be less expensive than conducting the litigation itself. If the examination produced damning evidence, one hopes the parties would settle rather than litigate, producing a net benefit for the estate. Yet, these cases will be rare because usually the professionals for the statutory entities (e.g., the DIP and the UCC) will argue that they are in the best position to make these determinations. Thus, the important question is whether the court and the system can trust these entities and their professionals to do so.

Creating a presumption for appointment in large cases would help flesh

[245]Of course, if one were to amend the Bankruptcy Code, it would make much more sense to do so in connection with comprehensive reform designed to reflect larger changes to the system, many of which involve its information functions. As I have argued elsewhere, phenomena such as the hedge fund and claims trading market simply did not exist in any meaningful way in 1978; yet they appear to have significant and growing influence over the reorganization process. *See* Lipson, *Shadow Bankruptcy, supra* note 32. The common denominator here and there is control of information in the reorganization of troubled firms. This is obviously a vital question. Examiners are one piece of that larger puzzle. R

[246]This paper has dealt only with large companies—those with assets in excess of $100 million and public securities. The suggestions offered here may not apply to smaller companies in chapter 11.

this out. As noted, it would force the participants, including statutory entities (the DIP and official committees) who oppose the appointment to explain why an examiner is not needed. If they have been fighting amongst themselves, or with other constituents (e.g., ad hoc committees of investors), they may have difficulty credibly explaining why an examiner would not help address those disputes or other matters that are left untended due to these internecine fights.

This suggests a second basis for appointing an examiner: if there is some conflict of interest that prevents the system from working in a reasonably fair and efficient way. As noted above, examiners have been used to address structural conflicts, for example when the creditors committee for a parent corporation cannot be expected to represent the interests of creditors of a subsidiary. A similar basis would be concern that professionals may, in some cases, be unable or unwilling to engage in a fair-minded assessment of causes of action due to low-grade conflicts. For example, they—and the case—may be captured by a secured lender whose credit facility includes a clause that treats suit against that creditor, or the appointment of an examiner, as an event of default. This would obviously pose a conflict that harms the estate.

More generally, repeat professional players (lawyers, turnaround consultants) in large cases may have distorted incentives.[247] Thus, these repeat players may avoid being aggressive in circumstances where they should be, or may be too aggressive in circumstances where they should not be, all influenced in subtle ways by concerns about their ability to obtain work in future cases. While this may not result in wholesale dereliction of fiduciary duty, it may distort the process. The question then becomes: how is a judge supposed to know when the process is being distorted rather than advanced?

Again, the presumption created by the proposed amendment to the statute contained in Appendix 3 would help. By creating a presumption that an examiner will be in the interests of the estate in cases involving misconduct, opponents will be forced to generate plausible explanations why an examiner appointment is not. There doubtless will be cases precipitated by allegations of fraud where the DIP and the UCC can do an effective job of rooting out and recovering for the misconduct, and thus where an examiner would add little direct benefit. It is equally clear, however, that the very limited use of examiners in fraud cases—they were requested in only nine of thirty-one cases involving fraud—suggests that something is keeping the parties from using this mechanism. If there are good reasons not to use an examiner when requested in a case involving fraud, we should know what they are.

The third, and perhaps most controversial, reason to use examiners involves their public benefits. Discussions about the use of examiners almost

[247] *See generally* LoPucki, Courting Failure, *supra* note 23. R

always focus only on their costs and benefits viewed from the perspective of stakeholders. If an examiner is not likely to produce greater recoveries to creditors, we should not have one, the thinking goes. The problem is that this ignores the larger public aspects of examinations, in particular, and reorganization, in general.

Congress (or at least Senator DeConcini) apparently believed that examiners would not only serve stakeholders, but also the broader public. Examiners, he stated, would be "*automatically*" appointed, in part, because "debtor and creditor interests, *as well as the public interest*, will be preserved and enhanced by [the Bankruptcy Code's examiner] provisions."[248] Moreover, while this is obviously a provocative claim, I believe reorganization serves important public functions: chapter 11 creates a public context through which we resolve financial distress.[249] Bankruptcy reorganization harnesses the power of the state, among other things, to strip or significantly impair (private) rights in contract, property, and tort through a judicial (public) forum.

Despite this, we increasingly treat chapter 11 as just another front in (private) battles for corporate control.[250] Private investors—who may not be public-spirited in this context—increasingly influence chapter 11 reorganizations, even as they may capture the many public benefits that flow from it, including information about the debtor and the discharge of (others') debts. Treating chapter 11 as though it were nothing but a market, however, is terrible policy. That view contributed to the abuses that outraged Justice Douglas and other system observers in the 1930s: In a system where everything is for sale, there is no reason to have confidence in the outcome of any given case.

Thus, reforms beginning with enactment of the Securities Exchange Act of 1934 sought to introduce greater public control of the reorganization process, chiefly through the intercession of the Securities and Exchange Commission and the mandatory ouster of management in large cases. Those two forms of public intervention have, however, been abandoned, leaving only examiners, judges and the United States Trustee system to police chapter 11. Without examiners, we have only judges, and the United States Trustee, both of whom are public servants whose work loads vastly outstrip their ability to police cases in the ways we might want.

The public benefit of examiners, then, is that they can create confidence in the system. How would they do this? Through deterrence and shaming.

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[248] *See* S 17404 (daily ed. Oct. 6, 1978) (statement of Sen. DeConcini) (emphasis supplied).

[249] *See* Lipson, *Shadow Bankruptcy*, *supra* note 32. *See also* Jonathan C. Lipson, *Debt and Democracy: Towards a Constitutional Theory of Bankruptcy*, 83 NOTRE DAME L. REV. 101 (2008). R

[250] *See* Lipson, *Shadow Bankruptcy*, *supra* note 32. R

We tend to forget today that bankruptcy was once a crime, a stigmatized act.[251] While recent amendments to the Bankruptcy Code have sought to re-stigmatize consumer bankruptcy, we largely exempt business bankruptcy from this normative judgment. The managers who lead their firms to failure have little to fear. If their compensation packages are properly designed they will collect a healthy (albeit smaller-than-anticipated) severance and go on about their business.[252] There is little cost for error in the executive suite because, except in extraordinary—i.e., criminal—cases, managers will usually walk away far better off than their employees and, in many cases, creditors. They will not be forced to explain what they did wrong or, by inference, be deterred from making similar mistakes in the future. There is no shame in corporate failure in part because there is no exposure. We neither learn from failure nor, through the trial of investigation, deter it.

Examiners could help to fix this. Used more frequently (and judiciously), examiners would not only explain bad practices that led to failure but also send a signal to future managers: if you fail, you will likely be examined, and the examination may lead to causes of action against you. At minimum, your errors would likely be subject to greater scrutiny than is currently the case.

Will this deter risk-taking? Perhaps. Is that bad? It depends on how the examiner is used. For cases caused by economic forces that had little to do with management quality, there is little reason for an examiner. In contrast, if there are credible allegations that pre-bankruptcy management made serious mistakes—did managers willfully ignore the risks, as in AIG?—and those mistakes are not being exposed by the chapter 11 process, there may be good reasons for an examiner.

To understand the difference in effect between having an examiner and not, one need look no further than the Bear Stearns, AIG and Lehman Brothers cases. Having not gone into chapter 11, we have little idea what really happened with Bear Stearns or AIG.[253] Was there actionable fraud? Were there intentional or constructive fraudulent transfers? Did directors or officers breach fiduciary duties? What did management really know, and when did they know it? For Bear Stearns and AIG we are unlikely to get anything resembling an independent and authoritative answer. No examiner exists to investigate and report on these questions.

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[251] *See* Lipson, *Debt and Democracy, supra* note 249. R

[252] The case of Rick Wagoner, former CEO of General Motors, provoked particular outrage. *See GM details payout to ex-chief Rick Wagoner*, L.A. TIMES, July 15, 2009, http://articles.latimes.com/2009/jul/15/business/fi-gm-wagoner15.

[253] For discussions of AIG and Bear Stearns, *see, e.g.*, Jonathan C. Lipson, *The Loophole that Became a Wormhole: Why the Fed Had to Bail Out AIG*, Concurring Opinions (Sept. 19, 2008), http://www.concurringopinions.com/archives/2008/09/the_loophole_th.html; Jonathan C. Lipson, *The BS that Didn't Bark: Why Bear Stearns Didn't (Doesn't) Go into Bankruptcy,* Concurring Opinions (Mar. 24, 2008), http://www.concurringopinions.com/archives/2008/03/lipson_on_the_b_1.html.

In *Lehman Brothers*, by contrast, we have an examiner who has undertaken a wide-ranging investigation, seeking answers to the question that many have asked about the credit crisis: why Lehman Brothers?[254] Examiner Anton Valukas's report was released as this article was going to press. At nine volumes, and more than 2000 pages, it was not possible to incorporate its analysis into this paper. But it appears to provide an extremely detailed discussion of many of the things that went wrong at Lehman Brothers. By contrast, without any bankruptcy examination for Bear Stearns, AIG, or the many others directly or indirectly bailed out by the federal government, we will have limited insight into why these companies made such egregious and costly errors. If an examiner is not a more common feature of cases precipitated by apparently serious wrong-doing, executives will have little to fear from conduct that is reckless or worse.

The proposed revision of § 1104(c) contained in Appendix 3 would enable courts to act on this public commitment. Because an examiner could be appointed where doing so would facilitate the reorganization process, considering costs and benefits, the modified language would be broad enough to encompass the economic interests of the debtor in question as well as the larger public interest. By structuring appointment as a presumption, however, there is a mechanism for parties to show that the costs to the estate of an examination outweigh the benefits, including those that might inure to the investing public.

This leaves a final question: Should examiners be mandatory, even if not sought by a party? One of the striking findings in this paper is that parties rarely ask for examiners. If examiners offer the foregoing (and other) benefits, should they not automatically be appointed, even if the parties do not ask for one? Should the system not impose examiners on these cases, since we cannot trust the parties to ask for them?

The proposed revision to § 1104(c) would not go this far. The reason is that if we more broadly define the legitimate grounds for an examiner, and reduce opportunities for gamesmanship, then those with an interest in understanding the debtor's failure—including the UST, the SEC, and public investors—should have an incentive to make requests when appropriate. They should not be deterred by the common judicial practice of ignoring requests to appoint examiners or by concerns that courts will react to such requests angrily, as was seen in the *Lyondell Chemical* case. In short, orienting exam-

[254] *See* Jeffrey McCracken & Michael Spector, *Fed Draws Court's Eyes In Lehman Bankruptcy*, WALL. ST. J. C1, Oct. 2, 2009; Order Directing Appointment of an Examiner Pursuant to Section 1104(c)(2) of the Bankruptcy Code, at 4, *In re* Lehman Brothers Holdings Inc, No 08-13555 (Bankr. S.D.N.Y. Jan. 16, 2009) (Docket No. 2569) (ordering examination to consider, among other things, "[t]he events that occurred from September 4, 2008 through September 15, 2008 or prior thereto that may have resulted in the commencement of the LBHI chapter 11 case"). *See also* note 12, *supra*.

iner requests and appointments around their legitimate policy goals—understanding failure and facilitating reorganization—should incline parties to request them more often, when appropriate.[255]

Thus, there is reason to change our approach to the use of examiners, but that does not necessarily mean that we should use them less. It means we should use them more intelligently, including by accounting for their larger public benefits. We should make them less tempting instruments of strategy and more effective tools for reorganizing firms in chapter 11.

In the meantime, however, it would appear that the bankruptcy system as it exists is generally reluctant to support such undertakings, for reasons of cost, case control, personal preference, and so on. Understanding failure, in other words, is not yet a priority of the system.

[255]Thus, this proposal would not directly address the observations set forth in Part 5.3 that the Bankruptcy Code's priority scheme, among other things, effectively deters investors from requesting examiners. Because investors may well have recourse to other sources of recovery, it is not clear that altering the existing priority scheme (that is, § 510) is necessary or appropriate. Thus, we can expect investors to continue to under-request examiners, although I would hope courts become more sensitive to the merits of these requests when made.

Table 2.2.2 Cases in which examiners were sought or appointed, with district, year of case filing, and name of examiner, if appointed and observable from dockets or pleadings.

Corporation Name	District	Year Filed	Examiner Appointed	Examiner Name
Acme Metals, Incorporated	DE	1998	No	
Adelphia Communications Corp.	NY SD	2002	No	
Al Copeland Enterprises, Inc.	TX WD	1991	No	
AM International, Inc. (1993)	DE	1993	No	
American Classic Voyages Co.	DE	2001	Yes	William P. Bowden
American Rice, Inc.	TX SD	1998	Yes	Ben B. Floyd
Ameriserve Food Distribution, Inc.	DE	2000	No	
Anchor Glass Container Corp. (1996) (Anchor Resolution Co?)	DE	1996	No	
At Home Corp	CA ND	2001	No	
ATA Holdings Corp.	IN SD	2004	Yes	Kenneth J. Malek
Baldwin Builders / Baldwin Building Contractors, L.P.	CA CD	1995	Yes	Michael S. Kogan
B-E Holdings Inc./Bucyrus-Erie Company	WI ED	1994	Yes	Salvatore A. Barbatano
Best Products Company, Inc. (1991)	NY SD	1991	Yes	Michael L Cook; Joel B. Piassick
Bonneville Pacific Corporation	UT	1991	Yes	Alan V. Funk
Brunos Inc.	DE	1998	Yes	Harrison J. Goldin
Cenvill Development Corp.	FL SD	1992	Yes	Jerry Markowitz
Cityscape Financial Corp.	NY SD	1998	Yes	Harrison J. Goldin
Coho Energy, Inc. (1999)	TX ND	1999	No	
Collins & Aikman	MI ED	2005	No	
Coram Healthcare Corp.	DE	2000	No	
Costilla Energy, Inc.	TX WD	1999	Yes	Ronald Hornberger
Covanta Energy Corp.	NY SD	2002	No	
Delta Air Lines, Inc.	NY SD	2005	No	
divine, inc.	MA	2003	Yes	Stewart Grossman
DVI Inc.	DE	2003	Yes	R. Todd Neilson
El Paso Electric Co.	TX WD	1992	No	
El Paso Refinery LP	TX WD	1992	Yes	
Enron Corp.	NY SD	2001	Yes	Harrison J. Goldin; Neal Batson
Envirodyne Industries Inc.	IL ND	1993	No	

Corporation Name	District	Year Filed	Examiner Appointed	Examiner Name
Fibermark Inc.	VT	2004	Yes	Harvey R. Miller
FLAG Telecom Holdings, Ltd	NY SD	2002	No	
Forcenergy Inc	LA ED	1999	No	
FoxMeyer Health Corp.	DE	1996	No	
Fruit of the Loom, Inc.	DE	1999	No	
Galey & Lord, Inc.	NY SD	2002	No	
Geneva Steel Company	UT	1999	Yes	Alan M. Singer
Global Crossing Ltd.	NY SD	2002	Yes	Martin E. Cooperman
Globalstar LP	DE	2002	No	
Grand Court Lifestyles, Inc.	NJ	2000	Yes	Brian T. Moore
Granite Broadcasting Corporation	NY SD	2006	Yes	
Gulf USA Corp.	ID	1993	Yes	Dennis Michael Lynn
Guy F. Atkinson Company of California	CA ND	1997	No	
Ha-Lo Industries	DE	2001	No	
Harrahs Jazz Co.	DE	1995	No	
Hawaiian Airlines Inc.	HI	2003	No	
ICH Corporation	TX ND	1995	No	
Imperial Sugar Company	DE	2001	No	
Interco Inc.	MO ED	1991	Yes	
IT Group, Inc. (The)	DE	2002	Yes	R. Todd Neilson
Jayhawk Acceptance Corp.	TX ND	1997	No	
Kitty Hawk, Inc.	TX ND	2000	No	
Koger Properties Inc.	FL MD	1991	Yes	
Leasing Solutions, Inc.	CA ND	1999	No	
Leisure Technology Inc.	CA CD	1991	No	
Lernout & Hauspie Speech Products NV	DE	2000	No	
Loews Cineplex Entertainment Corp	NY SD	2001	No	
Lomas Financial Corp. (1995)	DE	1995	No	
Loral Space & Communications Ltd.	NY SD	2003	Yes	Harrison J. Goldin
Medical Resources, Inc.	NY SD	2000	No	
Megafoods Stores, Inc.	AZ	1994	Yes	Clifton R. Jessup, Jr.
Metropolitan Mortgage & Securities Co., Inc.	WA ED	2004	Yes	Samuel R. Maizel

Corporation Name	District	Year Filed	Examiner Appointed	Examiner Name
Mid-American Waste Systems, Inc.	DE	1997	No	
Mirant Corp.	TX ND	2003	Yes	William K. Snyder
New Century Financial Corporation	DE	2007	Yes	Michael J. Missal
NewPower Holdings, Inc.	GA ND	2002	Yes	Rufus T. Dorsey
Northwest Airlines Corporation	NY SD	2005	Yes	
NRG Energy, Inc. (2003)	NY SD	2003	No	
Nu-kote Holding, Inc.	TN MD	1998	Yes	Randal S Mashburn
Owens Corning	DE	2000	Yes	
Payless Cashways, Inc. (2001)	MO WD	2001	No	
Peregrine Systems, Inc.	DE	2002	No	
PG&E National Energy Group	MD	2003	Yes	Daniel Scotto
Polaroid Corp	DE	2001	Yes	Perry M. Mandarino
Polymer Group, Inc.	SC	2002	Yes	Benjamin C. Ackerly
Refco Finance Inc.	NY SD	2005	Yes	Joshua R. Hochberg
Reliance Acceptance Group, Inc.	DE	1998	No	
SLI, Inc.	DE	2002	No	
Southern Pacific Funding Corporation	OR	1998	No	
SpectraSite Holdings, Inc.	NC ED	2002	Yes	David W. Boone
Stage Stores, Inc.	TX SD	2000	No	
Stellex Technologies, Inc.	DE	2000	No	
Sun HealthCare Group, Inc.	DE	1999	Yes	Kevin W. Pendergest
Trump Hotels & Casino Resorts Inc.	NJ	2004	No	
U.S.A. Floral Products, Inc.	DE	2001	No	
UAL Corporation (United Airlines)	IL ND	2002	Yes	Ross O. Silverman
US Airways, Inc. (2002)	VA ED	2002	No	
Washington Group International, Inc.	NV	2001	Yes	Jeffrey Truitt
Winn-Dixie Stores, Inc.	NY SD	2005	No	
Worldcom, Inc.	NY SD	2002	Yes	Dick Thornburgh
XO Communications, Inc.	NY SD	2002	No	

Table 3.2.2 Examiner Requests and Potential Estate Recoveries[256]

The following are some of the cases in which appointment of an examiner appeared likely to result in estate recoveries.

Case Name	Basis for examiner request	Explanation
The IT Group, Inc.	Proposed sale of assets for too little	A proposed sale of assets would not necessarily result in an avoidance action, but would directly affect distributions.
American Classic Voyages Co.	Substantive consolidation settlement proposed in plan	A consolidation of assets and liabilities in a plan will result in a net gain or loss to creditors of a given debtor depending on that debtor's position vis a vis the other entities in the consolidated group. Substantive consolidation may not necessarily increase the overall assets available to creditors, but it is an economic phenomenon that affects distributions. and is thus fairly characterized as an economic factor in an examiner request.
U.S.A. Floral Products, Inc.	Breach of fiduciary duty by directors and officers.	These claims will have an economic effect on the estate if they are claimed to be derivative claims (that is, claims of the debtor against the director and officers).
Owens Corning	Payment of asbestos claims	
Adelphia Communications Corp	Breach of fiduciary duties by officers and directors	

[256]This is only a sample, as I was not able to obtain pleadings for all cases in which an examiner was requested. Moreover, it is important to remember that in many cases, multiple grounds may have been stated in the request. It is not possible to know whether these economic, avoidance-like factors were as important as the non-economic factors.

Case Name	Basis for examiner request	Explanation
Mirant Corp.	Intercompany claims; fraudulent conveyance	The investigation and resolution of intercompany claims may not necessarily involve an avoidance action or increase estate recoveries on a net basis. A debtor whose claim against a non-debtor would not increase recoveries; a non-debtor whose claim against a debtor was cancelled, would. The possibility of reallocating value within debtor groups, however, suggested a direct economic correlation between the grounds for an examiner and an examiner request.
American Rice, Inc.	Avoidable pre-and- post-petition transfers	
DVI Inc.	Unspecified claims against directors and officers	
Metropolitan Mortgage & Securities Co., Inc.	Intercompany claims; legal malpractice claims	
Peregrine Systems, Inc.	Debtor obligation to indemnify directors and officers	
New Century Financial Corporation	Breach of fiduciary duty and professional negligence	
Halo Industries	Breach of duty; failure by management to pursue avoidance actions	
NewPower Holdings, Inc.	Mismanagement claims against insiders	
ATA Holdings Corp	Intercompany guarantees	Like intercompany claims, an examiner and resolution of intercompany guarantees may not increase aggregate assets, but may affect internal distributions
divine, Inc.	Breach of fiduciary duty by directors and officers	
PG&E National Energy Group	Intercompany claims	
Trump Hotels & Casino Resorts Inc.	Intercompany claims	

Case Name	Basis for examiner request	Explanation
Best Products Co., Inc. (1991)	Fraudulent conveyance claims	
Refco Finance, Inc.	Claims against insiders and professionals	
Loew's Cineplex Entertainment Corp.	Intercompany claims	
Enron Corp.	Breach of fiduciary duty; professional negligence	
Cityscape Financial Corp.	Proposed plan releases	Releases under the plan would have reduced or eliminated the estate's ability to recover from the released parties

The following are some of the cases in which appointment of an examiner did not appear likely to increase estate recoveries.

Case Name	Basis for examiner request	Explanation
Globalstar, LP	Movants disliked plan	
SLI, Inc.	Fraud	Movants asserted direct claims of fraud against directors and officers.
UAL Corporation (United Airlines)	Labor dispute	
Payless Cashways, Inc. (2001)	Objection to proposed liquidation of debtor	
SpectraSite Holdings, Inc.	Dispute about plan	
Grand Court Lifestyles, Inc.	Company complexity and plan disputes	
Washington Group International, Inc.	Questions about prepetition financial dealings	
Global Crossing Ltd	Accounting misstatements and SEC reporting issues	
XO Communications, Inc.	Proposed settlement of shareholder's fraud lawsuit	
Loral Space & Communications, Ltd	Valuation issues	
FLAG Telecom Holdings, Ltd.	Plan treatment and disclosure disputes	
Stage Stores, Inc.	Securities fraud	

Case Name	Basis for examiner request	Explanation
Geneva Steel Company	Debtor's going concern viability with respect to debtor in possession financing facility	
U.S. Airways	Securities fraud	
FiberMark	Intracommittee disputes; post-petition management issues	

Table 3.3

Regression Analysis
Examiner Requests

Examiner requests	Odds Ratio	Std. Err.	P>|z|	[95% Conf. Interval]
Net scheduled assets between $0 and $100 million	1.007175	.4775484	0.988	.397658, 2.550933
Net scheduled assets above $100 million	3.20747	1.341343	0.005*	1.413174, 7.279971
Trustee sought	5.753304	2.332972	0.000*	2.598687, 12.7374

n=255
95% confidence level

Trustee motion (percentage and [confidence interval])	No	Yes
Net scheduled assets $0-$100 million	.08609 [041732, .169269]	.351476 [.189003, .557589]
Net scheduled assets above $100 million	.230764 [.141597, .352992]	.633155 [.431721, .796795]

APPENDIX 1

Methodology—Quantitative Data

This Appendix briefly describes the methodology used in constructing the Examiners Database.

Dockets for cases in the Examiners Database cases were obtained in one of two ways. Through the PACER-Electronic Case Filing system[257] I obtained 571 electronic dockets in HTML or Word form. Five dockets in paper format were also obtained via a mass email request to lawyers and judges involved in BRD cases for which PACER dockets were not available.

The dockets were divided into three categories: (i) "full," (ii) "partial," and (iii) "pending." A docket is "full" where the case was closed as of the time the docket was downloaded, and it appeared that the docket contained continuous entries from case commencement to case closing. The Examiners Database has 549 full electronic or paper dockets. A "partial" docket is one where, although the case has been closed, the docket is missing large numbers of entries. The twenty "partial" dockets obtained were excluded from the Examiners Database. A docket was "pending" for cases not closed as of June 2007. The Examiners Database has twenty-seven "pending" dockets.

Being large cases, those in the sample had dockets with many entries, ranging from twenty-six to 31522, with a mean (median) number of entries of 2591.4 (1597.5).

The dockets were reviewed by two different sets of student workers who I trained, using a coding sheet that I prepared. The students completed a coding sheet for each docket reviewed. I and another research assistant reviewed the coding sheets to assure inter-coder reliability. In addition, I independently reviewed the dockets of the cases in which an examiner motion was made (or an examiner was appointed) as well pleadings from those cases, where available. The dockets as reviewed were stored in PDF form in order to preserve their integrity.

The information from the case coding sheets was recorded onto an Excel spreadsheet that contained certain data for the 576 cases in the Examiners Database originally collected by Professor Lynn LoPucki. The Examiners Database does not include all of the variables contained in the BRD; only those that appeared relevant to this study, including basic information about the case (debtor name, district, judge, year filed, duration, etc), the company (assets, liabilities, employees, etc), as well as the results of the case (whether a plan was confirmed, whether the debtor refiled, etc). The Examiners Database was then converted into a .dta file for use on Stata SE 10. Descriptive and inferential statistical analyses were performed using Stata SE

[257]http://pacer.psc.uscourts.gov/ (last visited June 25, 2008).

APPENDIX 2

Methodology—Interviews

Structured interviews were conducted with bankruptcy lawyers (five), current or former judges (five), former examiners (three)[258], and current or former bankruptcy system administrators (e.g., employees of the United States Trustee program) (six). The interview subjects were found by sending an email query to the lawyers and judges associated with the various cases in the BRD. The interviews had four parts: (i) demographic and personal information (e.g., race, gender, law school attended); (ii) views about the role of an examiner in a particular case (if applicable); (iii) views about the role of examiners in general; and (iv) views about the hypotheses investigated in this study. All of the interview subjects were asked permission to record the interviews. Only four so agreed. Notes were taken in all interviews, whether or not recorded.[259]

[258]Individuals who were currently working as examiners were unwilling to be interviewed.

[259]An exemption from an institutional review board was granted by Temple University

APPENDIX 3

Proposed Amendment to Bankruptcy Code § 1104(c)

(c) If the court does not order the appointment of a trustee under this section, then at any time before the confirmation of a plan, on request of a party in interest or the U.S. Trustee, and after notice and a hearing, the court shall order the appointment of an examiner if such appointment is in the interests of creditors, any equity security-holders, or the reorganization process.

(1) The appointment of an examiner shall be presumed to be in the interests of creditors, equity security holders or the reorganization process, if—

(A) there are ~~to conduct such an investigation of the debtor as is appropriate, including an investigation of any~~ allegations of fraud, dishonesty, incompetence, misconduct, mismanagement or irregularity in the management of the affairs of the debtor of or by current or former management of the debtor;~~(1) such appointment is in the interests of creditors, any equity security-holders, and other interests of the estate;~~ or

(B) the debtor had, as of the commencement of the case, $100 million or more in assets and was, within one year of such date, a reporting company under the Securities Exchange Act of 1934 or had, at any time, issued securities subject to the registration requirements of the Securities Act of 1933;[260] or

~~debtor's fixed, liquidated, unsecured debts, other than debts for goods, services or taxes, or owing to an insider, exceed $5 million.~~

(C) an examiner would otherwise facilitate the reorganization process, considering the costs and benefits of an examiner.

(2) The Court shall hear and decide a request under this subsection (c) no later than 60 days from the date it is made.

[260]Section 104 of the Bankruptcy Code should be amended to include this § 1104(c) in its inflation adjustment mechanism.