

**BUILDING ON BANKRUPTCY: A REVISED CHAPTER 14 PROPOSAL  
FOR THE RECAPITALIZATION, REORGANIZATION, OR LIQUIDATION  
OF LARGE FINANCIAL INSTITUTIONS**

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**THE RESOLUTION PROJECT**

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## I. INTRODUCTION

In 2012, building off of work first published in 2010, the Resolution Project proposed that a new Chapter 14 be added to the Bankruptcy Code, designed exclusively to deal with the reorganization or liquidation of the nation’s larger financial institutions.<sup>1</sup> This proposal was, in turn, the Resolution Project’s studied perspective on the most appropriate way to respond to the financial crisis of 2008 and the federal government’s role in it, highlighted by the bankruptcy of Lehman Brothers. There quickly emerged a consensus—certainly among our working group, but more widespread—that the institutions, and the government, lacked important tools to deal effectively with financially-distressed large financial institutions without the Hobson’s choice of either potential systemic consequences affecting the nation’s economy as a whole or a bail-out—a financial “rescue” of the institution so that it would not fail. Chief among the perspective that new tools were necessary was the widespread perception that bankruptcy, as it existed at that time, was simply not up to the task of resolving, according to the rule of law, such institutions in a fashion that would contain systemic effects.

This conclusion was the result of a number of subsidiary beliefs—some correct, some less-so. The bankruptcy process was too slow and cumbersome. The adversarial bankruptcy process was conducted before a judicial officer who might know the law, but

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<sup>1</sup> Kenneth E. Scott & John B. Taylor (eds.), Bankruptcy Not Bailout: A Special Chapter 14 (Hoover Institution Press 2012) (hereafter “**BNB**”); Kenneth E. Scott, George P. Schultz & John B. Taylor, Ending Government Bailouts as We Know Them (Hoover Institution Press 2010) (particularly Chapter 11, pp. 217-251).

didn't have the requisite economic or financial expertise or the power to consider systemic consequences. Bankruptcy had too many exclusions to deal effectively with a complex financial group (depository banks and insurance companies were wholly excluded; stockbrokers and commodity brokers were assigned to a specialized provision of Chapter 7).<sup>2</sup> And a series of amendments to the Bankruptcy Code, originally driven by ISDA and the Federal Reserve Board, had increasingly immunized counterparties on qualified financial contracts from the major consequences of bankruptcy, prominently including bankruptcy's automatic stay under Section 362.<sup>3</sup>

While members of the Resolution Project believed that a number of those criticisms were justified, we also believed that thoughtful revisions to the Bankruptcy Code could ameliorate or eliminate many of them, improving the prospect that our largest financial institutions—particularly with pre-bankruptcy planning—could be reorganized or liquidated pursuant to the rule of law (especially respecting priorities to ensure that losses fell where they were anticipated). Out of that grew our proposal for a special chapter designed for such financial institutions: a Bankruptcy Code Chapter 14.<sup>4</sup> Key features in that proposal included: (a) allowing an entire covered financial institution, including its non-bank subsidiaries, to be resolved in bankruptcy without the existing Bankruptcy Code's potpourri of exemptions; (b) the ability of the institution's primary regulator, who may be aware of potential systemic consequences otherwise not before a bankruptcy court, to file an involuntary petition, including based

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<sup>2</sup> These criticisms are outlined more fully in Kenneth E. Scott, George P. Schultz & John B. Taylor, *supra* note 1 at 218.

<sup>3</sup> Criticized both in *BNB*, *supra* note 1, at 45-46, and in David Skeel & Thomas Jackson, *Transaction Consistency and the New Finance in Bankruptcy*, 112 *Colum. L. Rev.* 152 (2012).

<sup>4</sup> See *BNB*, *supra* note 1.

on “balance sheet” insolvency, as well as to have standing to be heard as parties or to raise motions relevant to its regulation, including filing a plan of reorganization notwithstanding a debtor’s exclusive period and motions for the use, sale, and lease of property; (c) numerous changes to the protections afforded by existing bankruptcy law to holders of qualified financial contracts, especially derivatives and swaps, to ensure that they were treated according to their basic underlying attributes (that of secured liabilities, in the case of repos; that of executory contracts, in the case of derivatives and swaps); (d) provisions allowing, with designated protections against favoritism or bail-out, funding for the pre-payment of certain distributions to identified creditors; and (e) and the assignment of Chapter 14 cases and proceeding to designated Article III district judges, rather than to bankruptcy judges without the political independence provided by Article III.<sup>5</sup>

In proposing this, we wrote:

“We, the members of the Resolution Project group, believe it is possible through these changes to take advantage of a judicial proceeding—including explicit rules, designated in advance and honed through published judicial precedent, with appeals challenging the application of those rules, public proceedings, and transparency—in such a way as to minimize the felt necessity to use the alternative government agency resolution process recently enacted as a part of the Dodd-Frank Wall Street Reform and Consumer Protection Act. The new chapter could be adopted either in addition or as an alternative to the new resolution regime of Dodd-Frank.

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<sup>5</sup> For more detail, see *id.*, at 26-70.

“The crucial feature of this new Chapter 14 is to ensure that the covered financial institutions, creditors dealing with them, and other market participants know in advance, in a clear and predictable way, how losses will be allocated if the institution fails. If the creditors of a failed financial institution are protected (bailed out), then the strongest and most rapidly responding constraint on risk taking by the financial institution’s management is destroyed, and their losses are transferred to others.”<sup>6</sup>

Even with the passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010,<sup>7</sup> with its own Title II resolution process run by the Federal Deposit Insurance Corporation—the “Orderly Liquidation Authority”—we believe these changes to bankruptcy law remain vital to accomplish several of the announced goals of Dodd-Frank itself. First, Title I’s resolution plans—which we believe are an important part of pre-bankruptcy planning—require a focus on using bankruptcy as the standard against which their effectiveness will be measured.<sup>8</sup> And, second, invocation of Title II itself can only occur if the government regulators find that bankruptcy is wanting.<sup>9</sup> Unless bankruptcy can be seen as a viable alternative for the resolution of a large and complex Systemically Important Financial Institution (SIFI) in economic distress, (a) the resolution plans could technically be found not credible or facilitating an orderly liquidation (since they are to be based on bankruptcy) and (b) break-up, or use of Title

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<sup>6</sup> *Id.*, at 26.

<sup>7</sup> Pub. L. No. 111-203, 124 Stat. 1376 (hereafter “Dodd-Frank” or “Dodd Frank Act”).

<sup>8</sup> Dodd Frank Act, § 165(d).

<sup>9</sup> *Id.*, § 203(a)(1)(F) & (a)(2)(F); § 203(b)(2) & (3).

II of Dodd Frank, will be the only perceived effective responses to the “too big to fail” problem.<sup>10</sup>

Those remain important reasons for the adoption of many of the proposals the Resolution Project put forth in its original 2012 Chapter 14 proposal. That proposal, however, consistent with most of the thinking and work being done at that time, was focused on the resolution of an operating institution—which, in the case of a large financial institution, is usually at the subsidiary level of a holding company. Yet, in addition to the concerns with existing bankruptcy law, Title II, as enacted, had its own set of difficulties with effective resolution of any such financial institutions. Title II is designated the “Orderly *Liquidation* Authority,”<sup>11</sup> and Section 214(a) explicitly states: “All financial companies put into receivership under this subchapter shall be liquidated.”<sup>12</sup> A first-day lesson in a corporate reorganization course is that “understanding that financial and economic distress are conceptually distinct from each other is fundamental to understanding Chapter 11 of the Bankruptcy Code.”<sup>13</sup> Thus, what of a company whose going concern value exceeds its liquidation value? But if bankruptcy is perceived not to be up to the task and Title II required an actual liquidation of the business, there may be many cases in which the condition precedent for the use of Title II—that it will be more effective than bankruptcy—will not be met,

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<sup>10</sup> Reducing the size, and not just the complexity, of large financial institutions may be independently desirable, but that goal—if indeed it is one—should not be conflated with designing an appropriate mechanism for the effective resolution of a financial institution in distress.

<sup>11</sup> Dodd Frank Act §§ 206 & 208 (emphasis added).

<sup>12</sup> *Id.*, § 214(a). See also Thomas Jackson & David Skeel, *Dynamic Resolution of Large Financial Institutions*, 2 Harv. Bus. L. Rev. 435, 440-441 (2012).

<sup>13</sup> Barry Adler, Douglas Baird & Thomas Jackson Bankruptcy: Cases, Problems and Materials 28 (Foundation Press 4<sup>th</sup> ed. 2007)

and current bankruptcy will (or, under the terms of Dodd-Frank, should) be the (rather inefficient) result.

Since then, however, a sea-change in perspective has occurred.<sup>14</sup> Increasingly, the focus, in Europe as well as in the United States, has been on a reorganization or recapitalization that focuses, in the first instance, on the parent holding company (many or most of the assets of which are the equity ownership of its subsidiaries). Europe has focused on a “one-entity” recapitalization via bail-in<sup>15</sup> while the FDIC has focused in its SPOE proposal on a “two-entity” recapitalization.<sup>16</sup> Under the FDIC’s approach, a SIFI holding company (the “single point of entry”) is supposed to effectively achieve “recapitalization” of its business virtually overnight by the transfer of its assets and liabilities, except for certain long-term unsecured liabilities and any subordinated debt, to a new bridge institution. The bridge institution then is supposed to forgive intercompany liabilities or contribute assets to recapitalize its operating subsidiaries. Because of the splitting off of the long-term unsecured debt, the bridge institution, in the FDIC’s model, looks very much like a SIFI holding company following a European-like “bail in”; the major difference is that in the “bail in,” the SIFI holding company

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<sup>14</sup> A useful discussion of whether and how well Title II of Dodd Frank would have responded to the 2008 crisis—prior to the development of the SPOE proposal—is contained in David Skeel, *Single Point of Entry and the Bankruptcy Alternative* (forthcoming, Brookings 2014). Cf. Em Warren, *The Next Lehman Bankruptcy* (2014).

<sup>15</sup> Financial Stability Board, *Progress and Next Steps Towards Ending “Too-Big-to-Fail,”* Report of the Financial Stability Board to the G-20, at [www.financialstabilityboard.org/publications/r\\_130902.pdf](http://www.financialstabilityboard.org/publications/r_130902.pdf) (Sept. 2013); Thomas Huertas, Vice Chairman, Comm. Of European Banking Supervisors and Dir., Banking Sector, U.K. Fin. Services Auth., *The Road to Better Resolution: From Bail-out to Bail-in*, speech at The Euro and the Financial Crisis Conference (Sept. 6, 2010), at [http://www.fsa.gov.uk/library/communication/speeches/2010/0906\\_th.shtml](http://www.fsa.gov.uk/library/communication/speeches/2010/0906_th.shtml); Clifford Chance, *Legal Aspects of Bank Bail-Ins* (2011).

<sup>16</sup> Federal Deposit Insurance Corporation, *The Resolution of Systemically Important Financial Institutions: The Single Point of Entry Strategy*, 78 Fed. Reg. 76614 (Dec. 18, 2013) (hereafter “FDIC SPOE”).

before and after the recapitalization is the same legal entity (thus, the one-entity recapitalization), whereas in the FDIC’s SPOE proposal, the “recapitalized” bridge institution is legally different than the pre-SPOE SIFI holding company (thus, the two-entity recapitalization).

There are pre-conditions for making this work. Important among them are legal rules, known in advance, setting forth a required amount of long-term debt to be held by the holding company that would be legally subordinate to other unsecured debt—in the sense of being known that it would be “bailed-in” (in a one-entity recapitalization) or left behind (in a two-entity recapitalization).<sup>17</sup> And its effective use in Title II—as of this writing the FDIC has promulgated for comments a working document on its SPOE proposal<sup>18</sup>—needs to straddle the tension between Title II’s liquidation mandate (literally met because, following the transfer to the bridge company, the original holding company will be liquidated) and the notion of limiting financial contagion and using Title II only when its results are better than would occur in bankruptcy. That said, many recognize that the FDIC’s SPOE proposal for Title II of Dodd-Frank, consistent with parallel work in Europe, is a significant advance in terms of undermining the presumption that some firms are “too big to fail.”<sup>19</sup>

But it also comes with the defects that have always made us uncomfortable with a government agency run and dominated resolution proceeding. The FDIC retains discretion to prefer some creditors over others of equal rank, without limiting it to

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<sup>17</sup> See Kenneth E. Scott, *The Context for Bankruptcy Resolutions* (2014); see also John Bovenzi, Randall Guynn & Thomas Jackson, *Too Big to Fail: The Path to a Solution* (Bipartisan Policy Center, Failure Resolution Task Force May 2013).

<sup>18</sup> See FDIC *SPOE* *supra* note 16.

<sup>19</sup> See John Bovenzi, Randall Guynn & Thomas Jackson, *supra* note 17; David Skeel, *supra* note 14.



occasions where there is background legal authority (that will rarely occur at the holding company level), and at important points the FDIC, rather than the market, is making critical determinations regarding the bridge financial company and its equity.<sup>20</sup> Thus, the FDIC proposes that the bridge financial institution created in the SPOE process (treated as a government entity for tax purposes<sup>21</sup>) is effectively run, for a while at least, by the FDIC.<sup>22</sup> In addition, the FDIC's SPOE proposal relies on expert (and FDIC) valuations of the new securities that will form the basis of the distribution to the long-term creditors and old equity interests "left behind,"<sup>23</sup> and the FDIC retains the authority to distribute them other than according to the absolute priority rule so well known in bankruptcy law.<sup>24</sup>

Moreover, the SPOE proposal for Title II has the potential to create an even greater disconnect with both Title I of Dodd-Frank and the presumptive preference for use of bankruptcy in Title II. The first occurs because Title I's resolution plans are to be focused on what would happen to the financial institution *in bankruptcy*.<sup>25</sup> Without the ability to do a comparable recapitalization at the holding company level in bankruptcy, any resolution plan would not be focused on how to most effectively do such a recapitalization. And that would be particularly unfortunate because, without the kind of changes in bankruptcy law we propose, Title II—and its SPOE process—would become the default, not the extraordinary, process, which runs contrary to the express

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<sup>20</sup> See FDIC *SPOE*, *supra* note 14, at 76616-76618.

<sup>21</sup> Dodd Frank Act § 210(h)(10) ("a bridge financial company . . . shall be exempt from all taxation now or hereafter imposed by the United States, by any territory, dependency, or possession thereof, or by any State, country, municipality, or local taxing authority").

<sup>22</sup> FDIC *SPOE*, *supra* note 16, at 76617.

<sup>23</sup> *Id.*, at 76618.

<sup>24</sup> *Id.*, at 76619.

<sup>25</sup> Dodd Frank Act §165(d).

preference in Dodd-Frank for bankruptcy as a resolution process for financial institutions.<sup>26</sup>

Accordingly, the Resolution Project focused on what further changes might be appropriate in its Chapter 14 proposal to both (a) meet the original goals of an effective reorganization or liquidation of an operating company and (b) provide an effective mechanism that would accomplish the goals inherent in the one- or two-entity recapitalizations of the holding company suggested by bail-in and SPOE proposals. Again, the “bones” of a response to this are already inherent in the Bankruptcy Code. While it is probably the case that the original intent of Section 363 of the Bankruptcy Code—a provision providing for the use, sale, and lease of property of the estate—was to permit piecemeal sales of unwanted property, following the enactment of the Bankruptcy Code of 1978, Chapter 11 practice began, over time, to move in the direction of both (a) pre-packaged plans and (b) plans whose essential device was a going-concern sale of some or all of the business, leaving the original equity and much of the debt behind—with the proceeds of the sale forming the basis of their distribution according to the absolute priority rule.<sup>27</sup> It doesn’t fit perfectly, but it has been used, repeatedly, as a way of creating a viable business outside of bankruptcy while the claimants, left behind, wind up as the owners of the estate of the former business entity.

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<sup>26</sup> See *supra* note 9.

<sup>27</sup> David Skeel, Debt’s Dominion: A History of Bankruptcy Law in America 227 (Princeton 2001); Barry Adler, Douglas Baird & Thomas Jackson, *supra* note 13, at 466-467 (“between [1983 and 2003] a sea change occurred through which an auction of the debtor’s assets has become a commonplace alternative to a traditional corporate reorganization”).

Thus, the Resolution Project Working Group decided to “expand” its 2012 Chapter 14 proposal (which, for the purpose of clarity, we will designate the “original” Chapter 14) to include a direct recapitalization-based bankruptcy alternative—a “revised” Chapter 14. This revised Chapter 14 accommodates *both* a conventional reorganization of an operating company *and* a two-entity recapitalization of a holding company.<sup>28</sup> While there is a great deal of merit in considering ways of successfully implementing one-entity recapitalization, especially for the many financial companies that are not systemically important (and we have done so extensively amongst ourselves), in the United States, at least, it is simpler for SIFIs to build upon the two-entity recapitalization model. This is both because (a) Chapter 14 may operate in parallel to the FDIC’s SPOE proposal under Title II of Dodd-Frank and because Dodd-Frank itself looks to bankruptcy as the primary “competitor” to Title II<sup>29</sup> and (b) because it is, for a variety of reasons, easier to use the existing bankruptcy framework for a two-entity recapitalization than it is for a one-entity recapitalization.

While there are certainly overlaps with the way the original Chapter 14 proposal works—and would continue to work for conventional “reorganizations” of operating companies—the features that facilitate a two-entity recapitalization through bankruptcy are structurally somewhat distinct. They—together with the basic features of the original Chapter 14 proposal—are incorporated in the revised Chapter 14 proposal.<sup>30</sup> In this paper, we will, first, outline the basic features of the original

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<sup>28</sup> A section-by-section outline of this revised Chapter 14 proposal is contained in an Appendix, and will be referred to throughout.

<sup>29</sup> Dodd Frank Act § 203(a)(2)(F) & (b)(2).

<sup>30</sup> A Senate bill, S. 1861, 113<sup>th</sup> Congress, 1<sup>st</sup> Sess. (“The Taxpayer Protection and Responsible Resolution Act”) (December 1013) focuses on amending the Bankruptcy Code so as to incorporate

Chapter 14 proposal vis-à-vis the reorganization or liquidation of an operating company and point to where they (sometimes with modifications) are located in the revised Chapter 14 proposal. We will then focus on the additional provisions that form the basis for the two-entity recapitalization of a holding company that is at the center of the differences between the two versions.

But, first, a brief description of the differences between the two processes. The reorganization or liquidation of an operating company that was the focus of the original Chapter 14 proposal, and the “quick sale” recapitalization that is the major driver of the changes in the revised Chapter 14 proposal, trigger off of whether or not there is a motion for, and approval of a “Section 1405 transfer”<sup>31</sup> (as defined in our “section-by-section” proposal that forms an appendix to this chapter) within the first 48 hours of a bankruptcy case. If the court approves such a Section 1405 transfer, then the SIFI’s operations (and ownership of subsidiaries) shift to a new bridge company *that is not in bankruptcy*, in exchange for all its stock.

Through the transfer, this new bridge company will be (effectively) recapitalized, as compared to the original SIFI, by leaving behind in the bankruptcy proceeding long-term unsecured debt (called in the proposal “capital structure debt”) of the original SIFI. *After* the transfer, the debtor company remains *in bankruptcy* but is effectively a shell, whose assets usually will consist only of the equity interests in the bridge company and whose claimants consist of the holders of the long-term debt, any

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provisions for a two-entity recapitalization, without ancillary provisions for a more traditional reorganization or liquidation as contemplated by the original Chapter 14 proposal. We believe this is a positive step, though a complete bankruptcy solution should incorporate not just two-entity recapitalization provisions, but also provisions teed off of the original Chapter 14 proposal.

<sup>31</sup> Appendix, Section 2(6).

subordinated debt, and the old equity interests of the SIFI. It has no real business to conduct, and essentially waits for an event (such as an IPO for public trading in equity securities of the bridge company) that will value its assets (all equity interests in the new, recapitalized entity) and permit a sale or distribution of those assets, pursuant to bankruptcy's normal distribution rules, to the holders of the long-term and subordinated debt and original equity interests of the debtor (the original SIFI).

Thus, essentially, the revised Chapter 14 proposal includes four types of rules. One set, centered around the Section 1405 transfer, is specific to the mechanics of the two-entity recapitalization's transfer to the bridge company—keeping the other assets, debts, executory contracts, qualified financial contracts, and the like, “in place” and “intact” so they can be transferred to the bridge company. Another set of Chapter 14 rules, as noted above, is specific to the mechanisms of the reorganization of an operating company by keeping the SIFI a “going concern” during its reorganization. A third set of rules deals with the conceivable possibility that the Section 1405 transfer won't be approved, and thus provides for the transition from rules appropriate to the two-entity recapitalization to those appropriate to the reorganization (or liquidation) of the SIFI in bankruptcy. Finally, a fourth set of rules is common for all cases in Chapter 14, and thus applies to both a one-entity reorganization and a two-entity recapitalization. Many of these rules are those provided by Chapters 1, 3, 5, and 11 of the current Bankruptcy Code, which Chapter 14 expressly makes relevant (unless overridden by a provision of Chapter 14 itself) to all Chapter 14 cases, as augmented by the proposals suggested in our 2012 original Chapter 14 proposal.

## II. The original Chapter 14 proposal

The 2012 original Chapter 14 proposal centered around five basic areas where new provisions were added and existing bankruptcy provisions were modified. They were: (A) provisions applying to the creation of a new Chapter 14;<sup>32</sup> (B) provisions relevant to the commencement of a Chapter 14 case;<sup>33</sup> (C) provisions involving the role of the primary regulator in the bankruptcy proceeding;<sup>34</sup> (D) provisions involving debtor-in-possession financing;<sup>35</sup> and (E) provisions applicable to qualified financial contracts in Chapter 14.<sup>36</sup> The essence of these proposals is summarized next, although fuller treatment, of course, is contained in the 2012 original Chapter 14 proposal itself.

### *(A) Provisions applying to the creation of a new Chapter 14*

Recognizing that the provisions for a reorganization proceeding, in Chapter 11, and a liquidation proceeding, in Chapter 7, provided a solid starting point—together with the general provisions in Chapters 1, 3, and 5—Chapter 14 was built around the premise that a large financial institution (and its subsidiaries) would generally use those rules *except* where Chapter 14 was designed to explicitly change them. It, accordingly, called for a large financial institution<sup>37</sup> to concurrently file for both Chapter 14 and either Chapter 7 or Chapter 11.<sup>38</sup> Because of concerns about political independence, as well as judicial expertise, a Chapter 14 case would be funneled to pre-

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<sup>32</sup> BNB, *supra* note 1, at 27-33.

<sup>33</sup> *Id.*, at 34-38.

<sup>34</sup> *Id.*, at 39-40 & 44-45.

<sup>35</sup> *Id.*, at 40-44.

<sup>36</sup> *Id.*, at 45-66.

<sup>37</sup> See BNB, *supra* note 1, at 28; Appendix, Section 1(1).

<sup>38</sup> See BNB, *supra* note 1, at 29-30; Appendix, Section 1(2).

designated district judges in the Second and DC Circuits, who were expected to hear the cases themselves, rather than referring them to bankruptcy judges.<sup>39</sup> The district judges were given the express right to appoint a special master from a pre-designated panel to hear Chapter 14 cases and proceedings connected with a Chapter 14 case, as well as the designation of bankruptcy judges and experts to provide advice and input.<sup>40</sup>

*(B) Provisions relevant to the commencement of a Chapter 14 case*

To ensure that the entire financial institution could be dealt with in the Chapter 14 case, the original Chapter 14 proposal was to eliminate the exclusion in existing bankruptcy law for domestic and foreign insurance companies, as well as stockbrokers and commodity brokers, from Chapter 11 when a Chapter 14 case applied, although existing rules for the treatment of customer accounts would be made applicable to the bankruptcy proceedings of stockbrokers and commodity brokers and the SIPC (for stockbrokers) or the CFTC (for commodity brokers) would be given a right to be heard and file motions.<sup>41</sup> The original Chapter 14 proposal, however, did not change the current resolution practice of the FDIC over depository banks.<sup>42</sup>

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<sup>39</sup> See BNB, *supra* note 1, at 33; Appendix, Section 3(1).

<sup>40</sup> See BNB, *supra* note 1, at 33; Appendix, Section 3(1).

<sup>41</sup> See BNB, *supra* note 1, at 35-36; Appendix, Section 1(1).

<sup>42</sup> See BNB, *supra* note 1, at 36; Appendix, Section 1(1).

*(C) Provisions involving the role of the primary regulator in the bankruptcy proceeding*

In addition, a financial institution's primary regulator would be given the right to file an involuntary case against that financial institution and the right to do so, if contested, not just in the case of the institution generally not paying its debts as they become due, but also on the ground that either the financial institution's assets were less than its liabilities, at fair valuation, or the financial institution had an unreasonably small capital.<sup>43</sup>

Beyond the filing of an involuntary petition by a financial institution's primary regulator, the regulators of the business of a financial institution or any subsidiary thereof would have standing, with respect to the financial institution or the particular subsidiary, to be heard as parties and to raise motions relevant to their regulation.<sup>44</sup> The primary regulator would additionally be given the power, in parallel with the trustee or debtor-in-possession, to file motions for the use, sale, or lease of property of the estate pursuant to the procedures of Section 363 of the Bankruptcy Code.<sup>45</sup> And either the primary regulator or a creditors' committee would be permitted to file a plan of reorganization at any time.<sup>46</sup>

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<sup>43</sup> See BNB, *supra* note 1, at 37 & 38; Appendix, Section 2(3) & (4).

<sup>44</sup> See BNB, *supra* note 1, at 39; Appendix, Section 2(2) & (5).

<sup>45</sup> See BNB, *supra* note 1, at 40; Appendix, Section 2(2).

<sup>46</sup> See BNB, *supra* note 1, at 45; Appendix, Section 2(5).



*(D) Provisions involving debtor-in-possession financing*

The original Chapter 14 proposal would make it clear that DIP financing is available in Chapter 14, pursuant to Section 364's procedures and limitations, for financing that will permit partial or complete payouts to some or all creditors where liquidity or solvency of those creditors is a systemic concern, with those payments intended as "advances" for the likely payouts such creditors would receive in a liquidation or a reorganization at the end of the bankruptcy process. To ensure that this was not a back-door way of providing financial favoritism, these distributions would be subject to several burden of proof requirements, to be passed on by the district judge, as well as subordination of the claim of the entity providing such funding to the extent that the creditors receiving such distributions received more than they would have in the bankruptcy proceeding absent such funding. Moreover, if the government was the entity providing such funding, it would additionally be required to show that no private funding on reasonably comparable terms was available within the time frame required.<sup>47</sup>

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<sup>47</sup>See BNB, *supra* note 1, at 43-44; Appendix, Section 2(14). That provision, which adds a Section 1413, picks up the provisions regarding debtor-in-possession financing from the original Chapter 14 proposal. This provision is essentially for use in the original Chapter 14 proposal's reorganization of an operating entity model, that is carrying on an active business, and that needs liquidity in the bankruptcy proceeding, and perhaps may need, for financial stability purposes, prepayments to some claimants. It builds on the debtor-in-possession financing provisions of Section 364 of the Bankruptcy Code. In the case of a Section 1405 transfer (see Appendix, Section 2(6)), the judge will retain jurisdiction over the bridge company, on its application, sufficient to allow the Chapter 14 court to authorize for a limited period comparable funding, subject to the conditions, available to a debtor-in-possession under Section 1403.

*(E) Provisions applicable to qualified financial contracts in Chapter 14*

Rules written into the Bankruptcy Code over the past several decades have increasingly exempted counterparties on qualified financial contracts from many of bankruptcy law's special rules, including the automatic stay and preference law. Occasionally, these exemptions made underlying sense, but oftentimes, they do not. In the original Chapter 14 proposal, our Working Group proposed revisiting all these Code provisions, and treating the counterparties according to the underlying attributes of the contracts they possessed. In the case of counterparties on repo contracts, which are comparable to secured loans, the automatic stay would not apply in terms of netting, setoff, or collateral sales by the counterparty of cash-like collateral that is in its possession—each being an instance of rights that the counterparty could exercise without detriment to the debtor or its estate.<sup>48</sup> In the case of counterparties on derivatives, however, more significant short-term changes in existing law were proposed, again consistent with the idea that most derivatives were comparable to executory contracts, and should be treated as such. Thus, for three days, the counterparty would be subject to bankruptcy's automatic stay, so as to enable the debtor to exercise its choice between assumption and rejection of the derivative (although the debtor would need to accept or reject all of the counterparty's derivatives without cherry-picking). After three days, and unless the debtor had previously assumed the derivative, the counterparty would be free to exercise any rights it may have to terminate the derivative and, upon termination (either by action of the

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<sup>48</sup> See BNB, *supra* note 1, at 50-52; Appendix, Section 2(8).

counterparty or by rejection by the debtor), the counterparty will have the netting, setoff, and collateral sale rights of a repo counterparty in bankruptcy.<sup>49</sup>

Finally, counterparties on qualified financial contracts would be given no blanket exemption from the trustee's avoiding powers, including preference law, although preference law would be amended to provide a "two-point net improvement test" safe-harbor for certain payments and collateral transfers.<sup>50</sup>

### III. Incorporating a "Quick Sale" Recapitalization into Chapter 14

While most of these provisions continue to make sense, and apply as well to the reorganization or liquidation of an operating company, they—by themselves—are not focused sufficiently on a rapid recapitalization of a financial institution at the holding company level, in which—in the course of a very short period of time—it is intended that the financial institution, through the recapitalization, would (a) likely be solvent, (b) appear so to market-participants, and (c) be subject to market discipline, rather than be under the "protection" of a bankruptcy proceeding (or subject to the interference with market-based decisions by a judge overseeing the bankruptcy proceeding of the holding company).

Doing this requires several new provisions and counsels for some modifications in the proposals contained in the original Chapter 14 proposal. The most significant change in the revised Chapter 14 proposal is its focus on provisions implementing a quick recapitalization of a holding company, via a sale of its assets and liabilities (other

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<sup>49</sup> See BNB, *supra* note 1, at 56-60; Appendix, Section 2(8).

<sup>50</sup> See BNB, *supra* note 1, at 62-66; Appendix, Section 2(12).

than long-term unsecured debt and subordinated debt) to a bridge company immediately following the commencement of a bankruptcy case.<sup>51</sup> In essence, this quickly “removes” the assets from the bankruptcy process, in the form of a new, and hopefully clearly solvent, company, while leaving ownership rights of that company (as between the holders of the long-term or subordinated debt that is not transferred and the old equity holders who are also “left behind”) to be realized over time in the bankruptcy estate. In addition to requiring pre-identified long-term debt in sufficient quantity—a non-bankruptcy issue but critical to the ability of *either* Chapter 14 *or* the FDIC’s SPOE process to succeed<sup>52</sup>—it requires a series of rules permitting assets, liabilities, contracts, and permits to be transferred to the bridge company notwithstanding restrictions on transfer, or change-of-control provisions, or the like. In essence, a number of rules need to be in place to ensure that, but for the recapitalization, the bridge company has all of the rights and liabilities that the holding company had the moment before the commencement of the bankruptcy case. Virtually all of the new rules in the revised Chapter 14 proposal are designed to deal with this, although there are also some transitional rules, some changes in the original Chapter 14 proposal based on making the “quick sale” effective, and some (modest) changes in the original Chapter 14 proposal based on our current thinking.

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<sup>51</sup> Appendix, Section 2(6) (describing a Section 1405 “Special Transfer”).

<sup>52</sup> See Kenneth E. Scott, *supra* note 17.

(A) *The Section 1405 Transfer*

The heart of the change is what we have denominated the “Section 1405 transfer.”<sup>53</sup> This transfer is, in many ways, the key concept implementing the two-entity recapitalization idea in Chapter 14. It permits either the debtor or the Board (the two entities capable of filing a petition involving a “covered financial company”<sup>54</sup> that commences a bankruptcy case) to immediately make a motion for a transfer of the property of the estate, contracts, and liabilities (except for “capital structure debt”—our term for the debt that is left behind—and, of course, subordinated debt and equity)<sup>55</sup> of the debtor to a newly-created “bridge company.”<sup>56</sup> If the transfer is approved, every asset, liability, and executory contract of the debtor will be included in the transfer to the bridge company *except* for subordinated and capital structure debt (and equity). If the debtor owns collateral that secures a loan (other than via a qualified financial contract) with an original maturity of at least one year, upon its transfer pursuant to Section 1405 to the bridge company, the secured lender’s claim against the bridge company will be non-recourse.<sup>57</sup> However, through the prior definition of capital structure debt, that lender will, if the collateral is insufficient, have an unsecured claim for any deficiency in the Chapter 14 case.<sup>58</sup>

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<sup>53</sup> Appendix, Section 2(6).

<sup>54</sup> Defined in Appendix, Section 2(3) (and slightly modified from the original Chapter 14 proposal).

<sup>55</sup> Defined in Appendix, Section 2(3). A part of this definition of capital structure debt begins the idea, finished in Appendix, Section 2(6), that under-collateralized long-term secured debt will be treated as follows. (a) The secured portion of the debt will be transferred (along with the collateral) to the bridge company on a non-recourse basis and (b) the debt holder will retain an unsecured claim in the debtor’s bankruptcy for the remainder.

<sup>56</sup> *Id.*, Section 2(3).

<sup>57</sup> *Id.*, Section 2(3) & (6).

<sup>58</sup> *Id.*, Section 2(3).

The Section 1405 transfer motion shall be heard by the court no sooner than 24-hours after the filing (so as to permit 24-hour notification to the debtor, the 20 largest holders of the capital structure debt, the Board and the FDIC, and also the primary financial regulatory authority—whether US or foreign—with respect to any subsidiary whose ownership is proposed to be transferred to the bridge company in the Section 1405 transfer).<sup>59</sup> And, based on limited stays in other provisions in Chapter 14, the transfer decision essentially must be made within 48-hours after the filing.<sup>60</sup> The court can order the transfer only if it finds, or the Board certifies that it has found, that the bridge company adequately provides assurance of future performance of any executory contract, unexpired lease, or debt agreement being transferred to the bridge company.<sup>61</sup> The court must also confirm that the bridge company’s bylaws allow its board to be replaced, pursuant to a decision of the Chapter 14 judge after a notice and hearing for the equity owners of the bridge company (collectively, the debtor; individually, the holders of the long-term unsecured debt and, presumptively at least, the old holders of subordinated debt and equity interests of the debtor), and other parties in interest (such as the Board), during the first thirty days following the Section 1405 transfer to that bridge company.<sup>62</sup> Moreover, while the bridge company is not otherwise subject to the jurisdiction of the Chapter 14 judge following the transfer, that judge shall retain jurisdiction for six months, upon application of the bridge company, to award financing on the terms and conditions applicable to debtor-in-possession financing pursuant to

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<sup>59</sup> *Id.*, Section 2(6).

<sup>60</sup> See *id.*, Section 2(7) & (8).

<sup>61</sup> *Id.*, Section 2(6). If the certifications are challenged, the Chapter 14 judge, after appropriate proceedings, may award damages, *id.*, Section 2(4), and sovereign immunity is to that extent abrogated, *id.*, Section 1(3).

<sup>62</sup> *Id.*

Section 1413. This is done in order to provide access to liquidity in the (hopefully rare) occasions where market-based liquidity to the presumptively solvent bridge company is unavailable. It is limited to six months on the view that any market-based liquidity restrictions (whether local or global) will have dissipated or otherwise been dealt with by that time and the bridge company is thereafter on its own.

*(B) Commencing the Chapter 14 case*

While many of the commencement provisions in the original Chapter 14 proposal have been carried forward, there have also been some modest changes, based largely on the necessity for a decision on a Section 1405 transfer within 48-hours of the filing. While Chapter 14 itself is new, there will be provisions noting that, except where otherwise expressly provided by Chapter 14, the “non-substantive” chapters of the Bankruptcy Code (Chapters 1, 3, and 5) apply in Chapter 14, and that, again except where otherwise expressly provided by Chapter 14, the provisions of Chapter 11 apply in a case under Chapter 14.<sup>63</sup> While there is no provision for the “direct” use of Chapter 7, liquidations are permitted under Chapter 11 and a conversion to Chapter 7 under Section 1112 of the Bankruptcy Code is expressly allowed.<sup>64</sup> Because Chapter 14 generally incorporates the provisions of Chapter 11, there is no need for a “concurrent” filing under Chapters 14 and 11, as proposed in the original Chapter 14 proposal, although the substance is the same. (The current proposal is, in substance, similar to making the provisions of Chapter 14 a new subchapter of Chapter 11.)

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<sup>63</sup> *Id.*, Section 1(2).

<sup>64</sup> *Id.*, Section 1(3).

Chapter 14 can only be used by a “covered financial corporation,”<sup>65</sup> whose definition picks up institutions that are “substantially engaged in providing financial services or financial products” whose consolidated assets are more than \$50 billion, including subsidiaries that are neither banks (that currently are, and would remain, subject to FDIC resolution procedures), nor a stockbroker or commodity broker (which go into special Chapter 7 provisions).<sup>66</sup> (While subsidiaries of a covered financial corporation that are either themselves excluded banks, stockbrokers, or commodity brokers, cannot themselves file in Chapter 14, a parent institution owning such subsidiaries can nevertheless use Chapter 14.) In common with the original Chapter 14 proposal, there is no exclusion of insurance companies.<sup>67</sup> The definition of “covered financial corporation,” however, specifically excludes financial market infrastructure corporations (such as central counterparty clearing houses) as unsuited for the Chapter 14 proposal, even if they otherwise meet the definition of a covered financial corporation.<sup>68</sup>

As for the commencement of a Chapter 14 case, the revised Chapter 14 proposal picks up on, but modifies, the provisions for the commencement of a Chapter 14 case in the original Chapter 14 proposal. It continues with the ability of the SIFI itself (the debtor) to file a voluntary petition under Section 301 of the Bankruptcy Code.<sup>69</sup> It does not, however, permit three or more creditors of a SIFI to file an involuntary petition under Section 303 of the Bankruptcy Code, as this was thought to be both potentially

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<sup>65</sup> *Id.*

<sup>66</sup> *Id.*, Section 1(1).

<sup>67</sup> *Id.*

<sup>68</sup> *Id.*

<sup>69</sup> *Id.*, Section 2(4).



disruptive and unnecessary, particularly when a Section 1405 transfer might be the preferred solution, as the time-table for that determination simply doesn't accommodate time for a distinct hearing and resolution on the merits of the involuntary petition itself.<sup>70</sup> It does allow the Federal Reserve Board (the "Board") to file what is tantamount to a voluntary petition, in legal effect (e.g., the filing commences the case and constitutes an order for relief), if the Board certifies (and makes a statement of the reasons) that it has determined (after consultation with the Secretary of the Treasury and the FDIC) that the commencement of a Chapter 14 case is necessary to avoid serious adverse effects on the financial stability of the United States.<sup>71</sup> This substitutes the Board for the original Chapter 14 proposal's proposal regarding the primary regulator, makes several other changes in the standard, and makes the petition function equivalently to a voluntary petition (i.e., immediate order for relief) rather than an involuntary petition (that can be challenged before an order for relief). This was done with the thought that because of the very tight time constraint to approve a Section 1405 transfer (after notice and hearing), there simply wasn't time to have a meaningful insolvency hearing; in addition, once the filing was made, it was likely to be a "self-fulfilling prophecy." In its place is a Board certification regarding potential default and financial stability. However, the court would retain jurisdiction to subsequently hear and determine damages proximately caused by such filing, if it finds that the Board's certification was not supported by substantial evidence on the record as a whole (analogous in some respects to the damages provision of Section

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<sup>70</sup> See *id.*

<sup>71</sup> *Id.*

303(i)(2)(A)), so that there is an understanding that aggrieved parties (mostly the original equity holders of the debtor) could have *ex post* damage remedies.<sup>72</sup>

In terms of who oversees the Chapter 14 case, the original Chapter 14 proposal essentially displaced non-Article III bankruptcy judges with Article III district judges to handle Chapter 14 cases, and “funneled” all such cases to the Second and DC Circuits. We propose the same basic idea of using district judges, but have made some modifications in the original proposal. First, rather than funneling cases to the Second or the DC Circuits, it has at least one designated district court judge (selected by the Chief Justice of the United States) in each circuit who will be involved in Chapter 14 cases.<sup>73</sup> Ordinary venue rules (in 28 USC §1408) determine where the SIFI files (or the Board commences a case involving a SIFI). Because a designated judge, while within the judicial circuit, may not be within the judicial district where the Chapter 14 case is commenced (e.g., a ND Calif. designated judge with a SD Calif. venue of a Chapter 14 case), the provision deems the judge to be temporally assigned to the district in which the bankruptcy case is commenced.<sup>74</sup> (This decision to involve a judge from every judicial circuit, rather than funneling cases to the Second or DC Circuit, is responsive to likely political reaction by senators and representatives who focus on their own respective jurisdictions.) Moreover, the designated judge “goes with the case,” so if venue is changed, the district judge will be deemed temporarily assigned to the new

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<sup>72</sup> Section 2(4). Sovereign immunity is thereby abrogated. Section 1(3). Cf. Kenneth E. Scott, *supra* note 17.

<sup>73</sup> Appendix, Section 3. No need to exclude the Federal Circuit Court of Appeals, as that circuit has no district judges.

<sup>74</sup> *Id.*

district.<sup>75</sup> Second, it requires two-entity recapitalization cases—those involving a Section 1405 transfer—to be handled up to the point of the transfer by the designated district judge, but not necessarily thereafter (again, since most of the debtor’s “business” has been transferred to the bridge company).<sup>76</sup> In other cases—conventional reorganization cases of the type contemplated by the original Chapter 14 proposal—the designated district judge, as with the BNB proposal, must keep the case and proceedings without referral to a bankruptcy judge.<sup>77</sup> Referral to a bankruptcy judge, however, can occur if there is a decision to convert the case to Chapter 7 pursuant to Section 1112.<sup>78</sup> Third, the designated district judge can appoint a bankruptcy judge to assist the district judge as a special master.<sup>79</sup> Finally, because some circuits have appeals from bankruptcy judges go to the Bankruptcy Appellate Panel (consisting of non-Article III bankruptcy judges), and the remaining circuits may otherwise have appeals go to other district judges, this provision will require 28 USC §158(a) appeals from bankruptcy judges to go to the designated district judge.<sup>80</sup> (As usual, appeals from the designated district judge in cases and proceedings that haven’t been referred to a bankruptcy judge will go to the relevant court of appeals.)

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<sup>75</sup> *Id.*

<sup>76</sup> *Id.*

<sup>77</sup> *Id.*

<sup>78</sup> *Id.*

<sup>79</sup> *Id.*

<sup>80</sup> *Id.*

(C) *Role of Regulators*

In addition to the Board’s ability to file what is tantamount to a voluntary petition, as discussed above, the revised Chapter 14 proposal provides for several other roles for regulators.<sup>81</sup> First, it gives the Board standing to be heard on any issue relevant either to the regulation of the debtor by the Board or to the financial stability of the United States.<sup>82</sup> It gives the FDIC more limited standing—to be heard in connection with a Section 1405 transfer.<sup>83</sup> And it gives the primary financial regulator of any subsidiary (domestic or foreign) or its parent standing to be heard on any issue relevant to its regulation of that entity (including transfer of its ownership interests in a Section 1405 transfer as well as its ownership by the debtor in a reorganization rather than a two-entity recapitalization).<sup>84</sup> If there is a Section 1405 transfer, where—effectively—the bridge company continues as the “recapitalized” debtor (in a two-entity recapitalization), the Board’s regulatory interest should shift to the bridge company, so Chapter 14 provides that, after such a Section 1405 transfer, the Board’s remaining standing vis-à-vis the debtor is with respect to its equity ownership of the bridge institution.<sup>85</sup> If there is not a Section 1405 transfer, the Board, analogous to the primary regulator in the original Chapter 14 proposal, can file a plan of reorganization at any time. (In the typical Section 1405 transfer, we propose the appointment of a

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<sup>81</sup> References to the United States trustee as having a role are removed (Appendix, Section 2(2)), and our proposal essentially substitutes the (Federal Reserve) Board (a defined term from Appendix, Section 2(3)), thus, for example, giving the Board the power to move for the appointment of a trustee under Section 1104. While the original Chapter 14 proposal had provisions to give the primary regulator a role in the Chapter 14 proceeding, nothing exactly parallel to this exists in that proposal. Appendix, Section 2(5) follows, and modifies, the “regulator standing” proposal from the original Chapter 14 proposal.

<sup>82</sup> Appendix, Section 2(5).

<sup>83</sup> *Id.*

<sup>84</sup> *Id.*

<sup>85</sup> *Id.*

trustee immediately after the Section 1405 transfer, and thus all parties in interest, including the Board, are authorized to file a plan of reorganization without delay under Section 1121(c) of the Bankruptcy Code.)<sup>86</sup>

*(D) Provisions Related to Making the Section 1405 Transfer Effective*

As noted, at the heart of the two-entity recapitalization are two principles: First, that there is sufficient long-term unsecured debt to be “left behind” in the transfer to a bridge company so as to effectuate the recapitalization. Second, that the bridge company otherwise have the assets, rights, and liabilities of the former holding company. A number of provisions in the revised Chapter 14 proposal are designed to effectuate this latter principle.

First, there are provisions applicable to debts, executory contracts, and unexpired leases, including qualified financial contracts.<sup>87</sup> Conceptually, the goal of these provisions is to keep assets and liabilities “in place” so that they can be transferred to the bridge company (within a 48-hour window) and, thereafter, remain “in place” so that “business as usual” can be picked up the bridge company once it assumes the assets and liabilities. This requires overriding “ipso facto” clauses (of the type that would otherwise permit termination or modification based on the commencement of a Chapter 14 case or similar circumstance, including credit-rating agency ratings), and it requires overriding similar provisions allowing for termination or modification based on a change of control, since the ownership of the bridge company

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<sup>86</sup> *Id.*

<sup>87</sup> See generally Appendix, Section 2(7) & (8).

will be different than the ownership of the debtor prior to the bankruptcy filing.<sup>88</sup> It needs to be broader than Section 365 of the Bankruptcy Code, for at least two reasons. First, bankruptcy doesn't have a provision expressly allowing for the "transfer" of debt (although many debts are in fact transferred as a matter of existing practice under Chapter 11 "going concern sales"). Unlike executory contracts, which might be viewed as net assets (and thus something to "assume") or as net liabilities (and thus something to "reject"), debt is generally considered breached and accelerated (think "rejected") upon the filing of a petition in bankruptcy. But, if there is going to be a two-entity recapitalization, the bridge company needs to take the debt "as if nothing has happened." Thus, the revised Chapter 14 proposal has provisions (Sections 1406 and 1407) that are designed to accomplish that.<sup>89</sup> Second, Section 365 doesn't deal with change-of-control provisions; these provisions add that and extend it to debt agreements as well.<sup>90</sup>

A complexity is that the brief "stay" to allow the Section 1405 transfer needs itself to be terminated with respect to the termination or modification of any debt agreement if there is no Section 1405 transfer but, rather, a "regular" bankruptcy of the type contemplated by the original Chapter 14 proposal.<sup>91</sup> (Debts—liabilities that normally are deemed "breached" upon the filing of bankruptcy—are in this respect treated differently than executory contracts and unexpired leases, since the provisions of Section 362 and 365 of the Bankruptcy Code are expected to continue, as they do in other reorganization cases.)

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<sup>88</sup> *Id.*

<sup>89</sup> *Id.*

<sup>90</sup> *Id.*

<sup>91</sup> *Id.*, Section 2(7).

With respect to qualified financial contracts, similar rules apply. If there is a filing with a motion for a Section 1405 transfer, there is a stay of efforts to liquidate, terminate, or accelerate a qualified financial contract of the debtor or subsidiary or to offset or net out, other than rights that exist upon the normal maturation of a qualified financial contract.<sup>92</sup> (Unlike the detailed provisions in the qualified financial contracts proposal in the original Chapter 14 proposal, these provisions are distinct in that they apply rules that didn't apply (and continue not to apply) in the original Chapter 14 reorganization proposal, particularly with respect to repo counterparties and their ability to sell cash-like collateral.)

The stay applies for the period essentially until the Section 1405 transfer occurs, it is clear it won't occur, or 48 hours have passed.<sup>93</sup> Because of this interregnum, when there is a likelihood that the Section 1405 transfer will be approved, and all of these qualified financial contracts go over "in their original form" to the bridge company, there is a requirement that the debtor and its subsidiaries shall continue to perform payment and delivery obligations.<sup>94</sup> And, as long as the debtor and/or its subsidiaries are performing payment and delivery obligations, a counterparty is expected to comply with its contractual obligations as well; the failure to do so shall constitute a breach in accordance with the terms of the qualified financial contract.<sup>95</sup> Finally, if the filing of the bankruptcy case does not involve a motion for a Section 1405 transfer, or if the motion is denied, or if 48 hours pass, then the case will be considered to be a "conventional" reorganization case (rather than a two-entity recapitalization case), and

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<sup>92</sup> *Id.*, Section 2(8).

<sup>93</sup> *Id.*

<sup>94</sup> *Id.*

<sup>95</sup> *Id.*

thus the original proposed rules for qualified financial contracts in the original Chapter 14 proposal, shall come into play.<sup>96</sup>

Just as the principle of having the bridge company have the same rights, assets, and liabilities drives the provisions regarding debts, executory contracts, and unexpired leases just discussed (including qualified financial contracts), a similar provision is necessary to keep licenses, permits, and registrations in place, and does not allow a government to terminate or modify them based on an “ipso facto” clause or a Section 1405 transfer.<sup>97</sup>

Many avoiding power provisions use as a baseline what a creditor would receive in a Chapter 7 liquidation. That potentially brings into play various avoiding powers, such as preference law, against holders of short-term debt (such as commercial paper) who, in a Chapter 7 liquidation, might not be paid in full, but in a two-entity recapitalization under a Section 1405 transfer, will be paid in full. Thus, Section 1411 is designed to call off avoiding powers (other than Section 548 (a)(1)(A) of the Bankruptcy Code dealing with intentional fraud) in the case of a Section 1405 transfer, except with respect to transfers to or for the benefit of holders of long-term unsecured debt or subordinated debt (which is not transferred and is likely not to be paid in full) and transfers to the debtor’s equity holders (such as dividends made pre-bankruptcy while the SIFI was insolvent).<sup>98</sup>

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<sup>96</sup> *Id.*

<sup>97</sup> *Id.*, Section 2(10). We assume that the “name” of the bridge company will be close enough to that of the debtor that filed financing statements will remain effective under Article 9, Section 9-508, of the Uniform Commercial Code.

<sup>98</sup> Appendix, Section 2(12). In an ordinary recapitalization case (not involving a Section 1405 transfer), there are special avoiding power rules specified in the original Chapter 14 proposal for



Finally, while all of these provisions deal with those in a relationship with the holding company, similar provisions need to be implemented with respect to contracts and permits held by a subsidiary whose ownership interests are transferred to the bridge company. Thus, we provide that a counterparty to such contracts with the subsidiary cannot terminate, accelerate, or modify any executory contract, unexpired lease, or debt agreement based on either an anti-assignment provision or a change-of-control provision.<sup>99</sup> Nor may a party to an agreement with a subsidiary enforce a cross-default provision involving the debtor for the period during which a Section 1405 transfer motion is under consideration.<sup>100</sup> Again, these provisions, like Section 1406 and 1407, are designed to allow the two-entity recapitalization effected by a Section 1405 transfer to occur seamlessly with respect to the bridge company's ownership of the debtor's subsidiaries. Similarly, in the case of a subsidiary whose ownership is transferred to the bridge company in a Section 1405 transfer, those licenses, permits, and registrations cannot be terminated based on a "change-of-control" provision.<sup>101</sup>

*(E) Transitional Provisions Designed to Make the Section 1405 Transfer Effective*

Upon consummation of a Section 1405 transfer, the newly created bridge company will have no long-term unsecured debt (as capital structure debt has been left

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holders of qualified financial contracts. Those provisions have been incorporated in Appendix, Section 2(12) as well.

<sup>99</sup>*Id.*, Section 2(9). While these provisions affect the contracts of entities not themselves in bankruptcy, we believe they are fully authorized, if not by Congress' Article I bankruptcy power, then by application of the "necessary and proper" clause of Article I, as interpreted since *McCulloch v. Maryland*, 4 Wheat. 316 (1819). See also *United States v. Comstock*, 560 U.S. \_\_\_\_ (2010).

<sup>100</sup> Appendix, Section 2(9).

<sup>101</sup> *Id.*, Section 2(10).

behind with the debtor). It will, however, presumably have residual (equity) value—which is, indeed, the basis ultimately for payment to the debtor’s claimants that were not transferred to the bridge company. Whether the bridge will be able to meet legal and regulatory capital requirements with that equity value alone will depend both on ex post valuation and on whether the regulatory scheme requires (as we believe it must in order to effectuate a two-entity recapitalization in the first place) a certain amount of debt (and not just equity) for “loss absorbency” purposes. The bridge will initially have substantial capital (equity) on a book basis, but its initial book value may not be validated by market performance. Moreover, initially the bridge company will have no long-term unsecured debt—since that was left behind—and such debt may be crucial in terms of regulatory requirements.<sup>102</sup> The equity value in market terms will need to be sufficient for the bridge company, over time, to issue new long-term unsecured debt, but until that occurs, the bridge company is likely to be non-compliant with the debt side of minimum capital requirements. Thus, the revised Chapter 14 proposal proposes giving the bridge company a “window” in which it does not have to be in compliance with those capital requirements. That period of effective exemption from those capital requirements ends at the earlier of (a) the confirmation of the debtor’s plan of reorganization involving (as will usually be the case) the distribution of securities (or proceeds from their sale) of the bridge company or (b) the passage of one year from the Section 1405 transfer.<sup>103</sup> By the end of that window of exemption, the bridge company must be in compliance with relevant capital requirements, including those involving minimum long-term unsecured debt.

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<sup>102</sup> *Id.*, Section 2(11).

<sup>103</sup> *Id.*

Section 1145 of the Bankruptcy Code allows a reorganized debtor to issue securities pursuant to a plan of reorganization without complying with most securities laws; the idea being that the required disclosure in a plan of reorganization, under Section 1125, confirmed by a court, should substitute. Given that an envisioned end of a bankruptcy case of a debtor where there has been a Section 1405 transfer will be the sale or distribution of securities of the bridge company pursuant to a plan of reorganization, Section 1412 treats this situation as equivalent to the typical reorganization case involving securities of the debtor, and thus provides that a security of the bridge company shall be treated as a security of a successor to the debtor under a plan of reorganization, in cases where the court has approved the plan's disclosure statement as providing adequate information about the bridge company and the security—thus fitting it within the provisions of Section 1145.<sup>104</sup> Additionally, the exemption from any law imposing a stamp tax or similar tax, in Section 1146(a), applicable to securities issued pursuant to a conventional plan of reorganization, is provided to securities of the bridge company in connection with a confirmed plan of reorganization following a Section 1405 transfer.<sup>105</sup> (Importantly, unlike the ill-advised provision in Title II of Dodd-Frank that treats a bridge financial institution as equivalent for a government entity not subject to federal, state, or local tax,<sup>106</sup> there is no comparable provision for the bridge company created in a Section 1405 transfer. It is, and should be thought of as, a private company subject to no favorable tax considerations not applicable to its competitors. This is distinct from the issue of a

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<sup>104</sup> *Id.*, Section 2(13).

<sup>105</sup> *Id.*

<sup>106</sup> Dodd-Frank Act § 210(h)(10).

holding company's tax loss carry-forwards that should be treated as an asset that can be transferred to the bridge company in the Section 1405 transfer.)

If there is a Section 1405 transfer, the management, at least originally, of the bridge company is very likely to be the management of the entity that filed for bankruptcy. Given that, it would be a conflict of interest to have that same management having the status of the “debtor in possession” of the debtor, which is now the equity owner of the bridge company. As a consequence, and given (as noted in the prior numbered paragraph) that the debtor after the Section 1405 transfer isn't likely to be “operating” an ongoing business, there really is no need for prior management to be the “debtor in possession.”

Thus, Section 1414 requires the replacement of the debtor in possession with a trustee, appointed by the court after a notice and hearing, who shall be chosen from a pre-approved list of trustees.<sup>107</sup> This trustee will represent the estate before the judge, together with a creditors committee (consisting of representatives of the holders of capital structure debt), an equity holders committee (consisting of representatives of the former equity owners of the debtor), and other parties in interest.<sup>108</sup> The appointment of the trustee will also, importantly, permit “a party in interest” to file a plan of reorganization without needing to wait out (or call off) the exclusivity period for the debtor in possession in Section 1121(c) of the Bankruptcy Code. In cases not involving a Section 1405 transfer—that is to say, cases involving a “conventional” reorganization as contemplated by the original Chapter 14 proposal—this will permit,

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<sup>107</sup> Appendix, Section 2(15).

<sup>108</sup> *Id.*

but not require, the appointment of a trustee, but if a trustee is appointed, it will be from the same pre-approved list.<sup>109</sup>

In the situation of a Chapter 14 case where there is a two-entity recapitalization pursuant to a Section 1405 transfer, resolution of the Chapter 14 case will involve the debtor essentially awaiting a sale or distribution of equity securities of the bridge company that will be valued by the market. This distribution of stock or proceeds from it will form the basis of a plan of reorganization, including disclosure, solicitation of acceptances, a court hearing, and court confirmation of the plan (Sections 1123 – 1129 of the Bankruptcy Code). While the Bankruptcy Code does not expressly provide a time-table for these events, it seems appropriate, given the hoped-for market-based determination of the value of the bridge company's equity securities that will be distributed in a plan, together with the desire to conclude the bankruptcy case (and wind-down the debtor), to authorize explicitly a rapid time frame for solicitation, voting, and the court' hearing (and decision) on confirmation of the plan.<sup>110</sup>

*(F) Interface with Title II of Dodd-Frank*

Currently, in order to commence an orderly liquidation proceeding under Title II of Dodd-Frank against a “covered financial company,” where the Board of that company does not acquiesce or consent to the proceeding, the Secretary of the Treasury must petition the District Court for the District of Columbia.<sup>111</sup> The court is given 24 hours

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<sup>109</sup> *Id.*

<sup>110</sup> *Id.*, Section 2(16).

<sup>111</sup> Dodd-Frank Act § 202(a)(1)(A)(i).

to make a determination as to whether the Secretary’s findings (a) that the “covered financial company is in default or in danger of default” and (b) that the company “satisfies the definition of a financial company under Section 2019a)(11)” are “arbitrary and capricious”; if the court does not make a determination within that time frame, Dodd Frank provides that the petition is granted by operation of law.<sup>112</sup>

Given this very tight timetable, and given that if a Chapter 14 case was previously commenced there is already an involved district judge, the revised Chapter 14 proposal would amend Dodd-Frank by “substituting” the Chapter 14 district court (and judge) for the District Court for the District of Columbia.<sup>113</sup>

## APPENDIX

### PROPOSED BANKRUPTCY CODE CHAPTER 14 (REVISED):

Draft: July 7, 2014

#### SECTION 1: GENERAL PROVISIONS RELATING TO COVERED FINANCIAL CORPORATIONS

1) Amend **Section 101** of the Bankruptcy Code by adding a new subsection defining a “covered financial corporation” as any corporation with consolidated assets more than \$50 billion that is substantially engaged in providing financial services or financial products (other than financial market infrastructure corporations such as central

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<sup>112</sup> *Id.*, § 202(a)(1)(A)(v).

<sup>113</sup> Appendix, Section 4 (amending Dodd Frank Act § 202(a)(1)(A)(i)).

counterparty clearing houses), and any subsidiary of that corporation that both (i) is substantially engaged in providing financial services or financial products and (ii) is neither (a) an entity, other than a domestic insurance company, that is included on the lists in Section 109(b)(2) and (b)(3)(B) nor (b) a stockbroker (Section 741) nor (c) a commodity broker (Section 761).

2) Amend **Section 103** of the Bankruptcy Code to provide that (a) except as provided in Chapter 14, Chapters 1, 3, and 5 of the Bankruptcy Code apply in a case under Chapter 14 and (b) the provisions of Chapter 14 apply only in a case where the debtor is a covered financial corporation. Also, amend Section 103 to provide that, except as provided in Chapter 14, the provisions of Chapter 11 apply in a case under Chapter 14.

3) Amend **Section 106** of the Bankruptcy Code by adding Section 1403 to the list of sections where sovereign immunity is abrogated.

4) Amend **Section 109** of the Bankruptcy Code to provide that only a covered financial corporation may be a debtor under Chapter 14. Also, exclude the ability of a covered financial corporation to be a debtor under Chapter 11 or under Chapter 7 (unless, in the case of Chapter 7, it is pursuant to the application of Section 1112 in the Chapter 14 case).

5) Amend **Section 1506** of the Bankruptcy Code to provide that the court has the discretion not to enforce foreign home country stay orders, or not to issue orders barring domestic ring-fencing actions against U.S.-based assets, if the foreign home country has not adopted comparable provisions respecting ancillary proceedings in that foreign home country for U.S.-based home proceedings.

**SECTION 2: LIQUIDATION, REORGANIZATION, OR RECAPITALIZATION OF A COVERED FINANCIAL CORPORATION**

- 1) Amend the Bankruptcy Code by adding a new **Chapter 14** (“Liquidation, Reorganization, or Recapitalization of a Covered Financial Corporation”).
- 2) Add a **Section 1401**, “Inapplicability of other sections,” that provides that Sections 321(c) (allowing the U.S. trustee for the district to serve as a trustee) and 322(b) (essentially the same) do not apply to a case under Chapter 14. References to “the United States trustee” in Chapter 11 shall be deemed replaced by references to “the Board” (defined below).
- 3) Add a **Section 1402**, “Definitions for this chapter,” that defines (a) the “Board” as referring to the Board of Governors of the Federal Reserve System, (b) “bridge company” as the recipient of the transfer under Section 1405, whose equity interests are received by the Chapter 14 debtor in that transfer, (c) “capital structure debt” as unsecured debt (including the undersecured portion of secured debt), other than a qualified financial contract, of the debtor for borrowed money with an original maturity of at least one year; (c) “qualified financial contract” as contracts as defined in Section 101(25), (38A), (47), or (53B), Section 741(7), or Section 761(4), (5), (11), or (13).
- 4) Add a **Section 1403**, dealing with the “Commencement of a case concerning a covered financial corporation,” that permits a case to be commenced by the filing of either a voluntary petition by the debtor under Section 301 or by the Board if the Board certifies that it has determined, following consultation with the Secretary of the



Treasury and the FDIC, that the immediate commencement of a Chapter 14 case is necessary to avoid serious adverse effects on the financial stability of the United States. A filing by the Board with the requisite certification will be treated as equivalent to a Section 301 voluntary filing (that is, the commencement of the case will itself constitute an order for relief), except that, analogous to Section 303(i)(2)(A), the court, before or after a Section 1405 transfer, would retain jurisdiction so as, on motion and hearing, to determine any damages proximately caused by such a filing or transfer pursuant to Section 1405, if the court further makes the determination that the certifications required by either Section 1403 or Section 1405 were not supported by substantial evidence on the record as a whole.

5) Add a **Section 1404**, “Regulators,” permitting (a) the Board to be heard on any issue relevant to the regulation of the debtor by the Board or to financial stability in the United States, (b) the FDIC to be heard in connection with a transfer under Section 1405, (c) the primary financial regulatory agency (as defined in section 2(12) of Dodd-Frank) of any subsidiary of the covered financial corporation, or the primary financial regulator of any foreign subsidiary of the covered financial corporation or its parent, to be heard on any issue relevant to its regulation of that subsidiary. If there is a transfer under Section 1405, following that transfer, the Board can be heard only in connection with the debtor’s ownership of the bridge company. If there is not a transfer under Section 1405, then the Board is deemed a party in interest who can file a plan of reorganization at any time after the later of (a) the order for relief and (b) the failure to timely approve of a transfer under Section 1405, in a case where such transfer is sought.

6) Add a **Section 1405**, “Special Transfer of Property of the Estate, Contracts, and Debts.” On motion by the debtor or the Board at the time of the commencement of the case, and after a hearing, the court may order a transfer of the property of the estate, executory contracts, unexpired leases, and debt agreements, with the exception noted next, from the debtor to a bridge company. Neither capital structure debt and subordinated debt, nor equity interests may be transferred. All other assets and liabilities of the debtor shall be transferred to the bridge company if the court orders a transfer under this section. The transfer under this section shall specify that any debt for borrowed money that (a) is secured by collateral included in the transfer, (b) is not associated with a qualified financial contract, and (c) has an original maturity of at least one year, shall be non-recourse upon the transfer. Prior to the hearing, 24-hour electronic or telephonic notice shall be given to (a) the debtor, (b) the 20 largest holders of capital structure debt, (c) the Board and the FDIC, and (d) each primary financial regulatory authority, whether US or foreign, of any subsidiary whose ownership is proposed to be transferred, each of whom have standing, with respect to its particular regulatory jurisdiction, concerning the motion for a Section 1405 transfer. After the hearing, the court may not order the transfer unless it finds (or the Board certifies to the court that it has found) that the bridge company provides adequate assurance of future performance of any executory contract, unexpired lease, or debt agreement being transferred to the bridge company. In addition, the court may not authorize the transfer to the bridge company unless it determines that the by-laws of the bridge company will allow a thirty-day period in which the debtor, with the approval of the Chapter 14 judge after notice and a hearing, can determine the composition of the

board of the bridge company, notwithstanding the charter or by-laws of the bridge company or applicable non-bankruptcy law. Finally, while the court otherwise does not retain jurisdiction over the bridge company following the transfer, it does retain jurisdiction for six months, on application by the bridge company, for liquidity financing at the priority levels of, and on the conditions specified in, Section 1413.

7) Add a **Section 1406**, dealing with “Automatic Stay; Assumed Debt.” (I) Provide in this section that the filing of a petition operates as a stay, applicable to all entities, of the termination, acceleration, or modification of any debt agreement (other than a capital structure debt agreement or a qualified financial contract), executory contract (other than a qualified financial contract), or unexpired lease with the debtor, or of any right or obligation under any such debt, contract, lease, or agreement, solely because of a provision that is conditioned on (a) the insolvency or financial condition of the debtor at any time before the closing of the case; (b) the commencement of a Chapter 14 case; or (c) a change in a credit-rating agency rating (i) of the debtor at any time after the commencement of the case or (ii) of a subsidiary during the 48 hours after the commencement of the case, or (iii) of the bridge company or a subsidiary of the bridge company prior to the earlier of 90 days or the confirmation of a plan involving the debtor under Section 1129. The stay under this Section 1406 terminates, as to the debtor and with respect to any debt agreements with the debtor, upon the earliest of (a) a commencement of a Chapter 14 case without a motion for a Section 1405 transfer, (b) 48 hours after the commencement of the case, (c) the transfer of the debt agreement under an order authorizing a Section 1405 transfer, or (d) a determination by the court not to order a Section 1405 transfer. In addition, in the case of a subsidiary, the stay

terminates not only upon the foregoing conditions but by a determination by the court not to order the transfer of the interests of the debtor in the subsidiary to the bridge company.

(II) Provide, as well, in this section, that such a debt agreement, executory contract, or unexpired lease of the debtor, may be transferred (and thus assumed) by the bridge company under Section 1405 notwithstanding any provision in an agreement or applicable non-bankruptcy law that (a) prohibits, restricts, or conditions the assignment of such debt agreement, executory contract, or unexpired lease, or (b) terminates, accelerates, or modifies any such debt agreement, executory contract, or unexpired lease, based on a change in control in any party.

8) Add a **Section 1407**, “Treatment of Qualified Financial Contracts,” that provides that the filing of a petition to commence a Chapter 14 case that is accompanied by a motion for a Section 1405 transfer operates as a stay, notwithstanding Sections 362(b)(6), (b)(7), (b)(17), (b)(27), 555, 556, 559, 560, and 561, for the period specified in the stay duration in Section 1406, above, of the exercise of any contractual right (i) to liquidate, terminate, or accelerate a qualified financial contract of the debtor or a subsidiary or (ii) to offset or net out any termination value, payment amount, or the like except the exercise of contractual rights that arise upon the non-accelerated maturity of a qualified financial contract shall not be subject to the stay. During the period in which this Section 1407 stay is applicable, the debtor and its subsidiaries shall perform all payment and delivery obligations under a qualified financial contract that become due after the commencement of the case; if the debtor or a subsidiary, as the case may be, fails to perform any such obligation, the stay provided by this Section 1407

terminates. As long as the debtor and/or its subsidiaries are performing all payment and delivery obligations under a qualified financial contract that become due after the commencement of the case, the failure of a counterparty to perform its obligations under that qualified financial contract shall constitute a breach of such contract according to its terms. A Section 1405 transfer of a qualified financial contract to the bridge company may not occur unless (i) all qualified financial contracts between the counterparty and the debtor are transferred to the bridge company and (ii) all property acting as security to the qualified financial contract is likewise transferred to the bridge company. Upon the transfer of a qualified financial contract to the bridge company under Section 1405, notwithstanding any provision in the qualified financial contract or in applicable law, that qualified financial contract may not be terminated, accelerated, or modified, for a breach of a provision of the type identified in Section 1406 (I) between the time of the Section 1405 transfer until the conclusion of the Chapter 14 case involving the debtor. If there is not a request for a transfer under Section 1405, or if such transfer is not approved, or 48 hours from the filing of the petition have expired, then the provisions for qualified financial contracts originally outlined in “Chapter 14 version 1.0” in *BANKRUPTCY NOT BAILOUT* apply.

9) Add a **Section 1408**, “Subsidiary Contracts,” that provides that, notwithstanding any provision in an agreement or applicable non-bankruptcy law, an agreement of a subsidiary (including an executory contract, unexpired lease, or agreement under which the subsidiary issued or is obligated for debt) where the subsidiary’s ownership interests that are property of the estate are transferred to the bridge company in a Section 1405 transfer, such agreement may not be terminated, accelerated, or modified,

at any time after the commencement of the case, because of a provision prohibiting, restricting, or conditioning the assignment of the agreement or because of the change-of-control of a party to the agreement. Nor may a cross-default provision respecting the debtor in an agreement of the subsidiary be enforced in any case of the debtor involving a Section 1405 transfer motion during the earliest of 48 hours from the commencement of a case under this Chapter involving the debtor or the denial of a Section 1405 transfer motion.

10) Add a **Section 1409**, dealing with “Licenses, Permits, and Registrations,” that provides, notwithstanding any other provision of non-bankruptcy law, a Section 1405 transfer motion stays, for the period of time specified in Section 1406, any termination or modification of any Federal, State, or local license, permit or registration that the debtor or a subsidiary had immediately before the commencement of the case that is proposed to be transferred, based upon (i) the insolvency or financial condition of the debtor at any time before the closing of the case, (ii) the commencement of a case under this title, or (iii) a transfer under Section 1405. Following a Section 1405 transfer, all such licenses, permits, and registrations shall vest in the bridge company. In addition, where a subsidiary’s ownership interests that are property of the estate are proposed to be transferred to the bridge company in a Section 1405 transfer, a Section 1405 transfer motion stays, for the period of time specified in Section 1406 and thereafter if the subsidiary’s ownership interests that are property of the estate are transferred to the bridge company in a Section 1405 transfer, any termination or modification of any Federal, State, or local license, permit or registration that the subsidiary had

immediately before the commencement of the case, based on a change-of-control of the subsidiary.

11) Add a **Section 1410**, “Bridge Company Capital Requirements,” giving the bridge company an exemption from applicable debt or capital requirements (such as Basel III) until such time as (a) the confirmation of a plan of reorganization for the debtor that involves the distribution or sale of securities of the bridge company or (b) one-year from the Section 1405 transfer, whichever is earlier.

12) Add a **Section 1411**, “Avoiding Powers,” providing that in a case where there is a request for a Section 1405 transfer, and such transfer occurs, the avoiding powers in Sections 544, 547, 548(a)(1)(B), or 549, do not apply, except for transfers of (i) an interest of the debtor in property to or for the benefit of a holder of capital structure debt under Section 547 or (ii) an interest of the debtor in property to or for the benefit of a holder of equity of the debtor under Section 548(a)(1)(B). Additionally, if there is not a motion for a Section 1405 transfer or if such transfer is not approved, the provisions for the application of avoiding powers with respect to qualified financial contracts contained in BANKRUPTCY *NOT*BAILOUT apply.

13) Add a **Section 1412**, “Exemption from Securities Laws and Special Tax Provisions,” providing that, for purposes of Section 1145, a security of the bridge company shall be deemed to be a security of a successor to the debtor under a plan of reorganization if the court approves the disclosure statement for the plan as providing adequate information (as defined in Section 1125(a)) about the bridge company and the security. In addition, securities issued by the bridge company in connection with a

confirmed plan of reorganization shall have the protection from any law imposing a stamp tax or similar tax under Section 1146(a).

14) Add a **Section 1413**, “Debtor-in-Possession Financing,” that picks up the provisions regarding Section 364 in the original Chapter 14 version 1.0.<sup>114</sup>

15) Add a **Section 1414**, “Trustee in a Chapter 14 Case” that provides, if there is an approved Section 1405 transfer, then there shall be a trustee appointed by the court, after notice and a hearing, in lieu of the debtor in possession, for all purposes of the debtor after the Section 1405 transfer. The trustee shall be appointed by the court from a pre-approved list of trustees that has been determined by the Chief Judge of the Circuit. In other cases, a trustee, chosen from the pre-approved list of trustees, can be appointed pursuant to the provisions of Section 1104.

16) Add a **Section 1415**, “Solicitation, Acceptance, and Confirmation of a Plan,” providing that, in the case of a plan of reorganization proposed at or following the approval of a Section 1405 transfer, that a court may hold a confirmation hearing under Section 1128, within ten days of the circulation of the plan if voting for purposes of Section 1126 is sufficient, at the time of the hearing, to allow the court to make the determinations required by Section 1129.

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<sup>114</sup> Pursuant to Section 1405, these provisions will also be applicable to the bridge company. See Section 2(6).



### **SECTION 3: AMENDMENTS TO TITLE 28**

1) Provide, in **Section 298**, that, notwithstanding Section 295, the Chief Justice of the United States shall designate at least one district judge from each circuit to be available to hear a case under Chapter 14. And that district judge, again notwithstanding Section 295, shall hear a Chapter 14 case filed in that circuit, and shall be considered, for purposes of the case, to be temporally assigned to the district in which the bankruptcy case is commenced or any district to which the case is removed pursuant to 28 USC §1412. The district judge may not refer a motion for a Section 1405 transfer to a bankruptcy judge, notwithstanding Section 157. In a case in which there is not a motion for a Section 1405 transfer, or the motion is denied, the district court may not assign the case or proceedings under the case to a bankruptcy judge, unless there has been approved a motion to convert the case to Chapter 7 pursuant to Section 1112. In all cases where the district judge may not refer a case or proceeding to a bankruptcy judge, the district judge may appoint a bankruptcy judge as a special master. Appeals under Section 158(a) in a Chapter 14 case shall be heard by the assigned district judge.

### **SECTION 4: AMENDMENT TO DODD-FRANK WALL STREET REFORM AND CONSUMER PROTECTION ACT**

1) Amend **Section 202** by adding at the end of (a)(1)(A)(i) that, notwithstanding the provisions of this subsection, if a case has been commenced under Chapter 14 of Title 11, the relevant district court shall be the district court where the Chapter 14 case is

pending, and the judge overseeing the Chapter 14 case shall be assigned to hear and decide the order under (a)(1)(A) of this section.