ABI COMMISSION TO STUDY THE REFORM OF CHAPTER 11

First Public Meeting

April 19, 2012

Written Statement of James H.M. Sprayregen, P.C.

As an initial matter, I thank the American Bankruptcy Institute (ABI) for the invitation to serve on the Commission to Study the Reform of Chapter 11 of the United States Bankruptcy Code, and I appreciate the opportunity to submit this statement as part of the written record of our first public meeting.

By way of introduction, I am a partner at Kirkland & Ellis LLP and the head of our firm's restructuring practice group.[1] Over the course of almost 30 years of practice, I have represented essentially every constituency involved in the challenge of addressing the insolvent or otherwise distressed corporations that are the subject of Chapter 11. These have included major international and domestic companies, as well as their boards of directors, secured and unsecured creditors, asset purchasers, and investors, in both bankruptcy and out-of-court proceedings. I have counseled clients across a broad spectrum of industries, including manufacturing, technology, transportation, energy, media, and real estate. Some of these representations include the Chapter 11 cases of General Growth Properties, Inc., Innkeepers USA Trust, The Great Atlantic & Pacific Tea Company, MSR Resort Golf Course LLC, Sbarro, Inc., Visteon Corporation, Readers Digest Association, Inc., ION Media Networks, Inc., DBSD North America, Inc., United Airlines, United Artists Theatre Company, Chiquita Brands, Inc., and Trans World Airlines, Inc.

---

[1] The views expressed herein are solely my own, and are not offered on behalf of my firm or any other entity or organization.

In addition to the ABI, I am or have been a member of the National Bankruptcy Conference, the International Insolvency Institute, the World Bank Insolvency and Creditor Rights Task Force, the Turnaround Management Association, and the bankruptcy or insolvency divisions of the Chicago Bar Association, Illinois Bar Association, and Commercial Law League of America. I am the Vice President and member of the Executive Committee of the Board of Directors of INSOL International (INSOL), a global federation of turnaround specialists. In Spring 2013, I will become the President of INSOL. These varied domestic and international roles provide a comparative perspective into insolvency legal regimes, from which I hope and believe we can draw some useful guidance for further improvements to the U.S. Bankruptcy Code. Lastly, I have taught restructuring courses as an adjunct professor at both the University of Chicago Booth School of Business and the New York University School of Law, and I have testified before Congress and published articles on Chapter 11-related topics.

The ABI Commission to Study the Reform of Chapter 11 convenes at a pivotal time in the history of insolvency law in the United States. The development of our modern bankruptcy legal system has been uneven. Throughout the nineteenth century, Congress passed bankruptcy legislation in 1800, 1841, and 1867, in each instance repealing the legislation shortly after it was enacted. The first comprehensive bankruptcy legal regime was established by the enactment of the Bankruptcy Act of 1898. Common law filled the gaps in the 1898 Act, by fostering the development of the equity receivership paradigm as a mechanism for corporate reorganizations. The system of equity receiverships, which had its origins in the rehabilitation of railroad businesses, represents the genesis of modern reorganization law. The passage of the Chandler Act of 1938 marked the next significant milestone, codifying the notion of corporate reorganization.

Forty years later, as a result of an exhaustive review process by countless individuals and organizations, the Bankruptcy Reform Act of 1978 created Chapter 11, the modern corporate reorganization statute. Chapter 11 was intended to balance effectively the interests and needs of debtors and creditors, within the context of prevailing economic practices—and, at least initially, it successfully did so. For instance, the debtor in possession concept was adopted, thus allowing management (in most instances) to direct the debtor's reorganization, secured and unsecured creditors' rights were prioritized and protected, and the Office of the United States Trustee was created to advance the public interest. Chapter 11 provided Bankruptcy Courts and practitioners with the requisite tools to address massive tort liability cases, such as the bankruptcies of Johns Manville, A.H. Robins, and Dow Corning, as well as corporate fraud catastrophes, such as Enron, WorldCom, and Adelphia Communications.

However, 34 years have passed since the enactment of the Bankruptcy Reform Act of 1978. I began my legal career in 1985, following the 1984 amendments to the Bankruptcy Code. Between 1978 and 1984, and then between 1985 and 2005 (when the Code was most recently amended by the Bankruptcy Abuse Prevention and Consumer Protection Act), there have been myriad changes to Chapter 11. More specifically, since the 1978 Act, there have been dozens of amendments to the Code. But these amendments have been ad hoc, often targeted to address relatively discrete reforms, in reaction to the events of specific cases, and sought by stakeholders that have institutional interests into narrow aspects of Chapter 11. A more principled approach to revising the Code would study the needs and interests of debtors and all parties in interest, simultaneously and within the context of the entire Chapter 11 process.

To that end, it is manifestly evident that the fundamental nature of our modern economy, coupled with the events of the recent financial crises, mandate a holistic review of the efficacy of

Chapter 11 in its present form. Since 1978, advances in financial technology and creativity have allowed for the interconnected growth of markets, and rapid movement of capital, on an unprecedented, and perhaps unimaginable, scale. While that progress, and the wealth creation it fosters, is undeniably positive, it has not been balanced by commensurate advances in the legal infrastructure needed to buttress the downside of corporate failure. The Great Recession demonstrated that the fault lines of our economy run far deeper than we had anticipated. The boom and bust of today's business cycle requires an insolvency regime that appropriately facilitates "creative destruction," and provides for the orderly and equitable dislodgment and redeployment of productive assets. Chapter 11 can, and should, provide that orderly and invaluable framework. The effective restructuring of a debtor's financial and operational viability requires a balance between administrating a case quickly, and doing so completely and meaningfully—and Chapter 11 should accommodate a Bankruptcy Court's discretion to maintain that balance while safeguarding all stakeholders' interests.

A primary tenet of Chapter 11 is to allow a corporation to restructure itself in a manner that maximizes value for all corporate constituents. It is the statutory recognition of going-concern value—i.e., the understanding that many corporate enterprises are worth more reorganized than liquidated. To pursue that goal, Chapter 11 imposes an intricate system of checks and balances to ensure that no party in interest accumulates too much control over the reorganization process. For instance, the so-called "best interests of creditors" test, as codified in Section 1129(a)(7), provides that a proposed plan of reorganization cannot be confirmed unless it is demonstrated that every creditor or equity interest holder will recover at least as much under the proposed plan as that party would recover in a hypothetical liquidation.

In addition to providing financially distressed businesses with an opportunity to reorganize and avoid liquidation, Chapter 11 also advances the goal of protecting employees and retirees. For instance, since the introduction of Sections 1113 and 1114 into the Bankruptcy Code, judges, practitioners, lenders, labor unions, and authorized representatives have strived to fashion a successful negotiating process with respect to the treatment of labor and retiree obligations and collective bargaining agreements.

As we move further into the 21st century, we need to recalibrate Chapter 11 to advance as effectively as possible the notion that corporate failure is a natural and unavoidable feature of capitalism, and thus our global economy is best served by a Bankruptcy Code that promotes balance between predictability and flexibility. By appropriately embracing the fresh-start principle that provides distressed but viable businesses with the breathing spell needed to reorganize, while protecting creditors' rights during that process, Chapter 11 can and should operate to encourage an appropriate level of risk-taking inherent in an entrepreneurial environment.

The ABI Commission to Study the Reform of Chapter 11 represents an important opportunity to examine and modernize corporate bankruptcy law. I am honored to be part of this very worthwhile project and I look forward to the responsibilities and challenges it entails.