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Stephen J. Lubben
Excerpt
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INTRODUCTION

This book is something of a travel story. It recounts my journey through the whole of American business insolvency law. From Nevada's special provisions for insolvent campgrounds to the grand, and perhaps now endangered, provisions of the Dodd-Frank Act, signed into federal law by President Barack Obama on July 21, 2010, that created an Orderly Liquidation Authority (OLA) to address future Lehman Brothers.[1] It has been an eventful trip.

In the United States, most people equate insolvency with bankruptcy and the Bankruptcy Code. Business insolvency thus brings to mind comparatively familiar terms like "chapter 7" and "chapter 11," even if most nonbankruptcy lawyers only have the vaguest of notion of what those laws entail. The same lawyers will usually mumble something about the Bankruptcy *Act*, even though it has been the Bankruptcy *Code* since the days of a single *Star Wars* film and the Sex Pistols performing live in concert.

A commercial lawyer, especially if she does not practise at a place where billing rates exceed $1,000 per hour, might have some general familiarity with things like "assignments for the benefit of creditors," and even state court receiverships. Lawyers at law firms where the billing rates do reach such stratospheric levels might view these devices as unseemly relics of an earlier age.

Another group of lawyers will have experience with specialized insolvency regimes for specific types of businesses. The most obvious are

[1] Although the new president, Donald Trump, has launched several verbal attacks on Dodd-Frank, as this book goes to print (mid-2018), the law remains in place.

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those that proliferate among what we might broadly term the financial industry. Insurance companies, banks, credit unions, broker-dealers, and the like all have their own special rules for going bust. There could be more – the creation of specialized insolvency regimes for other businesses is only limited by the interests of legislators and the persistence of lobbyists. In the United States, there is also a theoretical limit on state insolvency laws that arises from the United States Constitution, but as we will see, that does not always hinder the creation of state insolvency laws, even if it renders them of dubious utility.

Before writing this book, I attempted to read the whole of American insolvency law. I believe I have largely succeeded. What follows is my attempt to make sense of all of it. It's not easy. Campground receiverships?

Of course, my ability to comprehend this great mass of law is limited by the abilities of an academic, sitting in a library in Manhattan, to understand the need for a special insolvency regime for grain silos, to again take but one example. But when such questions arose, I attempted to ask people who might know the answers, even if they did not necessarily know me. In many cases these people did respond, and I am grateful for their help.

This project has three principal goals. My first goal is to identify the points of commonality between the various insolvency statutes. Examining this common core is unheard of in a world where bankruptcy attorneys are regarded as quite distinct from banking or securities attorneys, despite the reality that each of them may be involved in an insolvency proceeding of a major American firm.

Second, I want to inspect the differences between these insolvency systems and to address any justification for the separation. If a broker-dealer liquidates in a proceeding before a federal bankruptcy judge, why does an insurance company liquidate in a state court, and a bank outside of court altogether? If we accept that banks are different, for example, and fail in different ways than "real economy" firms, does that justify keeping banks out of the traditional bankruptcy system?

My ultimate goal, as I discuss in the last chapter, is to begin a conversation about what our business insolvency law should look like. I view the insolvency system as a crucial, and often overlooked, part of the larger American entrepreneurial structure and consider that future

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laws might be better designed if we had a complete understanding of our law of failure. For example, Dodd-Frank might have provided for a clean break between OLA[2] and the Bankruptcy Code, instead of leaving large financial institutions sometimes subject to OLA, and sometimes subject to the Code. Lengthy, costly exercises like having financial institutions prepare "living wills" under the Bankruptcy Code are largely pointless if the big banks never liquidate under the Code.[3] Such a feature might have been omitted had Congress had access to a considered body of research on the goals and structure of our insolvency laws.

I end up concluding that there are two broad types of laws lurking within the general heading of "business insolvency law." First is the kind familiar to bankruptcy attorneys: laws that promote equal treatment of creditors, after sorting the creditors among classes. Exactly what that treatment will be is left to either a trustee applying a set of rules (in chapter 7 type mechanisms) or creditor bargaining (in chapter 11 like mechanisms). Most receiverships, assignments, and other general insolvency laws fit within this category, along with the Bankruptcy Code.

The other broad type of law gives one or more groups priority treatment over all others. We often see these laws in the financial institution context, but they exist elsewhere and they could, in theory, spread much further. Essentially, the legislature – federal or state – has decided that some groups of creditors should be spared the effects of a business's failure. These sorts of laws invoke the same basic language as the first type of insolvency laws, but their aims are different, as I note in the final two chapters.

Before we begin, I should also note that there are two clear approaches to a project such as this. One is to provide an encyclopedic account of all of American insolvency law. This would require dozens of volumes – the third and final edition of Ralph Clark's treatise on receiverships alone had four volumes, and he often neglected much of

[2] Orderly Liquidation Authority, in Dodd-Frank's Title II. I discuss this in more detail in Chapter 4.

[3] But not entirely pointless, if they lead to rationalization of the corporate structure, and perhaps a better understanding of how to head off financial distress.

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the fine detail. In case you had any doubt – perhaps, like the TARDIS, this little tome is bigger on the inside? – this is not the approach I have taken. Nobody would read such an endeavor, and no modern publisher would support it.

Instead, I try to distill the key points of the insolvency regimes I examine and present a broad overview of the terrain in an easily readable form. The goal is to explain the key differences and why each of the insolvency systems currently in place in American law does or does not make sense. This book will not make you an expert in any of the specific examples I discuss, because my aim is to alert readers to the variety of approaches that exist, rather than dwell on the minutiae.

So we begin.

But first, I would be remiss if I did not acknowledge the helpful comments I received along the way from Abbye Atkinson, Peter Clapp, Oscar Couwenberg, Melissa Jacoby, John Pottow, Richard Levin, Adam Levitin, Mike Simkovic, David Skeel, Joseph Sommer, and Jay Westbrook. As with everything I do, I owe special thanks to my wife, Jennifer Hoyden. Everything is better with her.

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