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Grassroots Shareholder Activism in Large Commercial Bankruptcies

Diane Lourdes Dick*

ABSTRACT

In early 2013, a group of similarly situated individuals gathered to discuss how they could defend themselves against a grave potential injustice. Time was of the essence, so they would need to act quickly to preserve their rights. Fortunately, their path to justice was already paved: the matter was pending in federal court, and each had standing to appear and be heard. But frustratingly, this seemingly well-paved path was barred to them. These individuals, who were technically parties to the proceeding, were virtually invisible

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to the court and largely disenfranchised in settlement negotiations. Striving to overcome these obstacles, they persisted in their efforts to unite and gain a collective voice in the proceedings. Throughout the summer, the group organized meetings, events and actions; they penned heartfelt letters to the judge and entered dozens of documents on the case docket. But despite these efforts, the court denied their requests for formal representation in the case and, shortly thereafter, approved a settlement that terminated their interests. Meanwhile, evidence surfaced to confirm their worst fears: others stood to profit handsomely from the settlement. Needless to say, these events have left a profoundly negative impression on these individuals. They believe that the legal system not only failed to protect their most basic procedural and substantive rights, but in fact served as an instrument of economic inequality and social injustice. These individuals were common shareholders of the iconic, publicly traded Eastman Kodak Company during its Chapter 11 bankruptcy reorganization. Many lost their life savings; all lost their trust in the U.S. financial markets and courts of law. This Article takes up their cause, providing the first empirical investigation and academic theorization of grassroots shareholder activism in large commercial bankruptcies.

I. INTRODUCTION

In recent years, individual shareholders of large and distressed publicly traded corporations in Chapter 11[1] bankruptcy have increasingly engaged in direct action and grassroots organization in their efforts to influence the restructuring.[2] By "direct action"[3] I mean personal involvement in the Chapter 11 case as a "party in interest,"[4] generally on a pro se basis, by filing motions, making formal appearances at court hearings, and taking other steps to be heard on issues pertaining to a corporate debtor's restructuring. By

1. 11 U.S.C. §§ 1101–1174 (2013) (providing for reorganizations and liquidations of bankrupt persons).

2. *See, e.g.*, Matthew Daneman, *Kodak Bankruptcy Plan Challenged by Shareholders, Retirees*, DEMOCRAT & CHRONICLE (May 10, 2013), http://roc.democratandchronicle.com/article/A2/20130511/BUSINESS/305100046/Kodak%20bankruptcy (describing direct action by individual shareholders in Eastman Kodak Company's bankruptcy); Bess Levin, *Day Trading Hipster Takes on David Tepper*, DEALBREAKER (June 13, 2011), http://dealbreaker.com/2011/06/day-trading-hipster-takes-on-david-tepper/ (reporting on the steps taken by an individual retail investor to appear and be heard in Washington Mutual's bankruptcy); Troy Racki, *WaMu Bankruptcy: Retail Investors Gain Representation*, SEEKINGALPHA.COM (Jan. 12, 2010), http://seekingalpha.com/article/182093-wamu-bankruptcy-retail-investors-gain-representation (describing grassroots efforts by Washington Mutual shareholders to defend the appointment of an official equity committee).

3. In the context of grassroots activism and social movements, the term "direct action" traditionally refers to nonviolent civil disobedience. *See generally* BARBARA EPSTEIN, POLITICAL PROTEST AND CULTURAL REVOLUTION: NONVIOLENT DIRECT ACTION IN THE 1970S AND 1980S (1993) (discussing nonviolent direct action to impact social change). But litigation can also be an instrument of direct action. *See* Lucie E. White, *Mobilization on the Margins of the Lawsuit: Making Space for Clients to Speak*, 16 N.Y.U. REV. L. & SOC. CHANGE 535, 539 (1987) (exploring "the potential of welfare litigation to become an occasion for the education and mobilization of poor people and their advocates").

4. In a Chapter 11 case, any "party in interest" may appear and be heard on any issue. 11 U.S.C. § 1109(b) (2013). "Party in interest" includes "the debtor, the trustee, a creditors' committee, an equity security's committee, a creditor, an equity security holder [of the debtor], or any indenture trustee." *Id.*

"grassroots organization"[5] I mean spontaneous and organic efforts to mobilize outside of the legal structures[6] designed to protect stakeholder interests in large commercial bankruptcies.[7] These activities include holding meetings, disseminating information, collaborating to conduct research and prepare filings, and donating time, money, and in-kind resources to advance restructuring outcomes that better preserve the rights of non-insider holders of common stock in the debtor corporation.

Individual shareholders are engaging in direct action and grassroots organization because they are almost entirely disenfranchised once a corporation enters bankruptcy.[8] In the case of an insolvent company, the board of directors no longer owes its fiduciary duties exclusively to the corporation and its shareholders; instead, directors are generally expected to maximize the value of the firm for the benefit of creditors, who have also become residual stakeholders of the firm.[9] Even when the debtor is solvent, managers typically focus their efforts on gaining consensus to a Chapter 11 plan, often making significant concessions to creditors at the expense of shareholders.[10] Further compounding matters, the U.S. Trustee and bankruptcy courts have grown hostile to shareholder requests to appoint official equity committees in Chapter 11 proceedings,[11] making it very difficult for widely dispersed shareholders to come together and gain a seat at the bankruptcy negotiation table.[12]

5. The term has been studied most often in the fields of political science and sociology. *See generally* JEFFREY STOUT, BLESSED ARE THE ORGANIZED: GRASSROOTS DEMOCRACY IN AMERICA (2010) (exploring modern-day progressive grassroots political organizing in the United States); ROBERT A. GOLDBERG, GRASSROOTS RESISTANCE: SOCIAL MOVEMENTS IN 20TH CENTURY AMERICA (1996) (using sociological theory and historical analysis to explore 20th century social movements).

6. These traditional legal structures include the debtor's management, official committees appointed to represent similarly-situated claimants in bankruptcy, ad hoc groups and dominant shareholders, the bankruptcy judge, the U.S. Trustee, and the SEC. *See infra* Part II (considering the limitations of traditional legal structures that have the potential to advance the interests of shareholders).

7. By "large commercial bankruptcies," I mean those commercial bankruptcy cases that come within the working definition of "mega cases" used by the Administrative Office of the U.S. courts: "extremely large case[s] with: (1) at least 1000 creditors; (2) $100 million or more in assets; (3) a great amount of court activity as evidenced by a large number of docket entries; (4) a large number of attorneys who have made an appearance of record; and (5) regional and/or national media attention." LAURA B. BARTELL & S. ELIZABETH GIBSON, A GUIDE TO THE JUDICIAL MANAGEMENT OF BANKRUPTCY MEGA-CASES 5 (2d ed. 2009).

8. This observation is made in David L. Barrack et al., *Shareholders Retain Significant Rights in Bankruptcy: The Fight for Control of U.S. Energy Systems, Inc.*, J. CORP. RENEWAL (2008), *available at* http://www.turnaround.org/Publications/Articles.aspx?objectID=9658.

9. *See infra* Part II.A (discussing the possible shift in the corporate board's fiduciary duties in times of corporate financial distress for the benefit of the firm's creditors). The principle is well-established in Delaware corporate law. *See, e.g.*, N. Am. Catholic Educ. Programming Found., Inc. v. Gheewalla, 930 A.2d 92, 103 (Del. 2007) (denying a right for creditors to bring direct fiduciary claims against directors, but recognizing the directors' duty to maximize the value of the insolvent corporation for the benefit of all those having an interest in it).

10. *See infra* notes 64–66 and accompanying text (highlighting the debtor's "tendency to pacify large creditors, with whom the debtor expects to do business, at the expense of small and scattered public investors").

11. *See infra* Part II.B (explaining the prevailing view that official equity committees are in most cases unnecessary and inefficient).

12. The importance of assembling coalitions in order to gain a seat at the negotiation table is discussed in Michelle M. Harner & Jamie Marincic, *Behind Closed Doors: The Influence of Creditors in Business Reorganizations*, 34 SEATTLE U. L. REV. 1155, 1158–59 (2011).

In this way, bankruptcy law magnifies the severe collective action obstacles that shareholders already face under modern corporate law.[13] But in Chapter 11, the stakes are often much higher. This is because the modern commercial bankruptcy reorganization process relies upon party consensus rather than judicial edict,[14] meaning that claimants and interest holders must have a seat at the negotiation table if they ever hope to defend their rights and influence the proceedings.

In an attempt to overcome these and related challenges, a grassroots shareholder movement has been taking shape.[15] Angry investors from around the world, who stand to lose all or part of their life savings in prominent corporate bankruptcies, have taken to the Internet to parse through the debtor's financial information, critique the proposed restructuring plan and exchange information and expertise.[16] Many file their own motions and supporting documents with the bankruptcy court,[17] and some even attend hearings and make formal appearances in the case.[18] Meanwhile, others dedicate their time and

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13. Collective action principles are generally explored in ELINOR OSTROM, GOVERNING THE COMMONS: THE EVOLUTION OF INSTITUTIONS FOR COLLECTIVE ACTION (1990); MANCUR OLSON, THE LOGIC OF COLLECTIVE ACTION: PUBLIC GOODS AND THE THEORY OF GROUPS (1965). These and related theories are thoughtfully applied to the corporate shareholder context in ANDREAS JANSSON, COLLECTIVE ACTION AMONG SHAREHOLDER ACTIVISTS (2007).

14. Diane Lourdes Dick, *The Chapter 11 Efficiency Fallacy*, 2013 BYU L. REV. 759, 766 (2013).

15. It is difficult to ascertain exactly when the shareholder collective action this Article describes initially became part of the corporate governance landscape. Similar grassroots activities were earlier observed among retirees of large companies. *See generally* Jeff May, *AT&T Retirees Protecting Benefits*, DUKEEMPLOYEES.COM - DUKE ENERGY EMPLOYEE ADVOCATE (June 13, 2003), *available at* http://www.dukeemployees.com/retirees5.shtml ("Retirees of many of the largest U.S. companies have been banding together to try to protect their benefits."). Such grassroots activism by retirees featured prominently in the Enron bankruptcy proceedings. Given that the shareholders I encountered predominantly use the Internet to stay abreast of the case, gather additional information, and interact with each other, I suspect that this particular form of grassroots activism is a relatively new phenomenon, which has likely picked up steam in the wake of the recent financial crisis and ensuing recession.

16. *See, e.g., Eastman Kodak Co. Message Board*, YAHOO! FINANCE, http://finance.yahoo.com/mb/EKDKQ/ (last visited Sept. 15, 2014) (reflecting thousands of posts by self-described individual shareholders of Eastman Kodak Company, exchanging information and analyzing financial and legal consequences at each stage of the proceedings); WMI Holdings Corp. (WMIH) Message Board, INVESTORS HUB, http://investorshub.advfn.com/WMI-Holdings-Corp-WMIH-11133/ (last visited Sept. 15, 2014) (same, albeit with respect to the Washington Mutual Chapter 11 case).

17. *See, e.g., In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y.) (reflecting letters, objections and other filings by individual shareholders on the docket); *In re* Washington Mut., Inc., Case No. 08-12229 (Bankr. D. Del.) (same).

18. For instance, individual common shareholders attended and participated in hearings during Eastman Kodak Company's Chapter 11 case. *See, e.g.*, Transcript of Hearing, *In re* Eastman Kodak Co., 2013 WL 4413300, Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. Aug. 20, 2013) (on file with the author); Transcript of Hearing, *In re* Eastman Kodak Co., 2013 WL 4413300, Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. Aug. 5, 2013) (on file with the author); *see also* Levin, *supra* note 2 (describing objections and court appearances by an individual retail investor (the "day-trading hipster") in the Washington Mutual Chapter 11 case); Objection to the Plan of Reorganization, filed by Nate Thoma, *In re* Washington Mut., Inc., Case No. 08-12229 (Bankr. D. Del. Nov. 19, 2010), ECF No. 6058 (articulating the investor's arguments).

resources to maintaining websites,[19] transcribing information, and fundraising to support the needs of similarly situated shareholders.[20]

For the most part, these individuals are not part of the economic elite or the so-called one percent.[21] They are working- and middle-class persons who invested their life savings in the stock market through retail brokerages or employer-sponsored retirement accounts. And, while they clearly possess courage and conviction to intervene in the federal bankruptcy proceedings of America's largest corporations, these shareholders are not affluent persons with great influence.[22] Rather, they are ordinary people who recognize that they are disenfranchised but refuse to be silenced; they hope that their collective efforts will augment their individual voices.[23]

From a shareholder-rights corporate theoretical perspective,[24] grassroots shareholder activism is an expression of democratic values in corporate governance; it is the quintessential exercise of voice rather than exit.[25] In particular, grassroots shareholder activists believe that today's commercial debtors are not necessarily insolvent such that the restructuring process ought to presumptively exclude equity owners; rather, they believe that large corporate debtors are able to creatively shield substantial economic wealth and use it to reward preferred corporate stakeholders.[26] In this way, these activists strive to

19. *See, e.g.*, Kodak General Board, KODAK-SHAREHOLDERS.COM, http://kodak.boards.net/ (last visited Sept. 15, 2014) (establishing a web forum for individual shareholders of Eastman Kodak Company during the pendency of the company's Chapter 11 case). Similarly, the now-defunct website, www.ghostofwamu.com, served as an important information exchange tool throughout the Washington Mutual bankruptcy case. *See, e.g.*, *'Ghost of WaMu' posts 61-page expert valuation report*, BVWIRE (Oct. 20, 2011), *available at* http://www.bvlibrary.com/BVWire/bvwireArticles.aspx?docRef=1972 ("Started in 2009 by a former WaMu shareholder who was 'burned' by the FDIC's seizure of the bank's billion-dollar assets, the site has served as a central repository for the latest filings.").

20. Efforts to collect funds to pay attorneys and expert witnesses are detailed on a Kodak shareholder message board. *See, e.g.*, diamondrockvegas, *Our Man Ahsan Zia wills set up a PayPal Account / GooglePay*, Kodak General Board, KODAK-SHAREHOLDER.COM, http://kodak.boards.net/thread/6175/ahsan-wills-paypal-account-googlepay (last visited Nov. 29, 2014). One Eastman Kodak Company shareholder contributed $2000 to hire an attorney to represent individual common shareholders in the company's Chapter 11 case. Interview with Nancy Bo (Aug. 20, 2014) (on file with the author).

21. For an interactive resource, see Phil Izzo, *What Percent Are You?*, WALL ST. J. (Oct. 19, 2011, 6:00 AM), http://blogs.wsj.com/economics/2011/10/19/what-percent-are-you/.

22. In other words, they are not necessarily those generally described in MARTIN GILENS, AFFLUENCE AND INFLUENCE: ECONOMIC INEQUALITY AND POLITICAL POWER IN AMERICA (2013).

23. The phrase "collective outbursts" describes collective behavior that is more transitory in nature, happening in response to some event or situation. In contrast, "collective movements" are "collective efforts to modify norms and values, which frequently (but not always) develop over long[] periods." NEIL J. SMELSER, THEORY OF COLLECTIVE BEHAVIOR 3 (1962). The grassroots shareholder activism described in this Article can be viewed as collective outbursts manifesting in a given case.

24. *See, e.g.*, Lucian A. Bebchuk, *The Myth that Insulating Boards Serves Long-Term Value*, 113 COLUM. L. REV. 1637, 1641 (2013) (referring to the author's longstanding view that corporate law should protect and promote "shareholder rights and engagement").

25. *See generally* ALBERT O. HIRSCHMAN, EXIT, VOICE, AND LOYALTY: RESPONSES TO DECLINE IN FIRMS, ORGANIZATIONS, AND STATES (1970) (advancing a theory of economic, political, and social dynamics within organizations).

26. Of course, to the extent distributions are made even though more senior claimants have not been made whole, they are in violation of bankruptcy's absolute priority rule. 11 U.S.C. § 1129(b) (2010). *See also* Ralph Brubaker & Charles Tabb, *Bankruptcy Reorganizations and the Troubling Legacy of Chrysler and GM*, 60 U.

underscore certain structural problems that are inherent in the commercial restructuring process under Chapter 11: the tendency for certain privileged stakeholders with existing market power to take control of the restructuring, shield wealth and extract excess returns at the expense of other constituents;[27] the failure of bankruptcy law's most vital safeguards to fully take into account the intangible assets that drive modern restructurings, such as intellectual property, litigation claims, and valuable tax attributes;[28] and the inherent difficulty of valuing complex corporations and their assets.[29]

Of course, grassroots shareholder activism might also be viewed as a nuisance, hindering an already protracted and costly commercial bankruptcy process. Nonetheless, direct action, grassroots organization, and collective outbursts by angry, disenfranchised shareholders should be understood as inevitable in today's large commercial restructurings. This is because the legal process, as determined under U.S. bankruptcy and corporate laws, harbors enormous structural strain.[30] Chapter 11 relies primarily on negotiated settlement by powerful players, pitting the interests of average working- and middle-class persons who own corporate stock against the interests of much larger stakeholders, such as corporate insiders, dominant creditors, and activist venture capital funds that specialize in distressed investments.

Individual shareholders serve as instruments of social change when they attempt to organize and obtain a voice in Chapter 11 proceedings. Their efforts complement a global social movement that decries unjust corporate enrichment and seeks to hold corporations and others in positions of power accountable to ordinary citizens.[31] But grassroots shareholder activism threatens the interests of those who have grown accustomed to controlling corporate restructurings with little to no interference by widely dispersed common shareholders. It also threatens to impose additional costs upon already distressed companies, even potentially impairing long-term access to credit. For these reasons, the topic deserves careful consideration. Although recent scholarly attention has been given to

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ILL. L. REV. 1375, 1391 (2010) (referring to the absolute priority rule as "one of the most central, fundamental distribution-value protections of a chapter 11 plan"). But if the corporation is solvent, any residual equity rightfully belongs to the company's historic shareholders. The "magic" of bankruptcy is that through a confirmed Chapter 11 plan, and without necessarily making a clear determination of the debtor's solvency, a debtor may wipe out existing shareholders, make certain distributions, and emerge from bankruptcy with new shareholders, who receive the company's residual value and the right to enjoy any future increases in value.

27. Dick, *supra* note 14, at 765.

28. Diane Lourdes Dick, *Bankruptcy's Corporate Tax Loophole*, 82 FORDHAM L. REV. 2273, 2307 (2014). Professor Michelle Harner recently tackles the problem of "soft variables" in commercial restructurings in Michelle M. Harner, *The Value of Soft Variables in Corporate Reorganizations*, 2015 U. ILL. L. REV. (forthcoming 2015).

29. *See* Kerry O'Rourke, *Valuation Uncertainty in Chapter 11 Reorganizations*, 2005 COLUM. BUS. L. REV. 403, 414–27 (2005) (highlighting the difficulty of valuing equity interests in a reorganized debtor).

30. On the role of structural strain, see SMELSER, *supra* note 23, at 47–66.

31. While there is no evidence linking grassroots shareholder activists to the Occupy Wall Street (OWS) movement, their actions clearly advance the broader goals identified by OWS in its Principles of Solidarity. *See* WRITERS FOR THE 99%, OCCUPYING WALL STREET: THE INSIDE STORY OF AN ACTION THAT CHANGED AMERICA 22 (2011) (setting forth a narrative account of the movement). *See generally* DAVID GRAEBER ET AL., WE ARE MANY: REFLECTIONS ON MOVEMENT STRATEGY FROM OCCUPATION TO LIBERATION (2012) (providing a social movements analysis of the OWS movement).

large and powerful activist shareholders,[32] on one hand, and to less powerful "citizen shareholders,"[33] on the other, grassroots activism by individual common shareholders in large commercial bankruptcies has never been thoroughly investigated. In striving to fill this void in the literature, this Article addresses the following questions: Why are individual common shareholders resorting to grassroots organization and direct action? What specific methods do they use? Finally, are direct action and grassroots activism effective ways to influence Chapter 11 case outcomes? In practical terms, given that equity security holders are often perceived as "wiped out" as a consequence of a company's bankruptcy filing,[34] non-insider shareholders probably have little to lose from direct action and grassroots activism. But do they actually benefit from these attempts to organize and influence the proceedings? And, from a normative perspective, should the law discourage or facilitate their participation in the case?

This Article addresses these and related questions through empirical investigation. It focuses mainly on a single case study, the recent bankruptcy reorganization of the iconic, publicly traded Eastman Kodak Company.[35] In particular, it analyzes qualitative data gathered through direct observation of grassroots shareholder activism, in-depth interviews with several activist shareholders, and dozens of written documents produced and disseminated by activists. Such in-depth, qualitative analysis of grassroots shareholder activism contributes to a broader understanding of corporate relations, even beyond the bankruptcy arena. In particular, the study sheds new light upon the essential characteristics of equity investment in the modern corporation,[36] such as the separation of ownership and

32. Studies tend to focus on investors, such as hedge funds, who acquire large stakes in publicly traded corporations. *See, e.g.*, Bebchuk, *supra* note 24 (considering arguments for and against insulation of boards from powerful, activist shareholders). *See generally* April Klein & Emanuel Zur, *Entrepreneurial Shareholder Activism: Hedge Funds and Other Private Investors*, 64 J. FIN. 187 (2009) (analyzing activist interventions by powerful, activist shareholders); Edward B. Rock, *The Logic and (Uncertain) Significance of Institutional Shareholder Activism*, 79 GEO. L.J. 445 (1991) (exploring activism by large institutional investors). For a recent comparative analysis considering the roles hedge funds play in corporate governance, see Alexandros Seretakis, *Hedge Fund Activism Coming to Europe: Lessons Learned from the American Experience*, 8 BROOK. J. CORP. FIN. & COM. L. 438 (2014).

33. Professor Anne Tucker uses the term to describe individuals who are indirectly invested in publicly traded corporations through defined retirement plans. *See, e.g.*, Anne Tucker, *Retirement Revolution: Unmitigated Risks in the Defined Contribution Society*, 51 HOUS. L. REV. 153, 153 (2013); Anne Tucker, *The Citizen Shareholder: Modernizing the Agency Paradigm to Reflect How and Why a Majority of Americans Invest in the Market*, 35 SEATTLE U. L. REV. 1299, 1302–06 (2012).

34. The point is succinctly made by a popular investing columnist: "The most likely outcome [of a Chapter 11 case] is for the old stock to be canceled, effectively being wiped out, at the end of the bankruptcy process." Paulo Santos, *Understanding Bankruptcies As An Investor*, SEEKINGALPHA.COM (Jan. 11, 2012, 2:30 AM), seekingalpha.com/article/318759-understanding-bankruptcies-as-an-investor.

35. *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y.). The parent company and its U.S. subsidiaries filed voluntary petitions for relief under Chapter 11 of the U.S. Bankruptcy Code in the U.S. Bankruptcy Court for the Southern District of New York. The cases were jointly administered as Case No. 12-10202 (ALG) under the caption "*In re* Eastman Kodak Company." The debtors operated their businesses as debtors-in-possession under the jurisdiction of the bankruptcy court. All references in this Article to the "debtor" in the context of Eastman Kodak Company refer collectively to all of the affiliated debtor entities.

36. By "modern corporation," I mean that which is described by Adolf Berle and Gardiner Means in their foundational work on post-industrial corporate organization. ADOLF BERLE & GARDINER MEANS, THE MODERN CORPORATION AND PRIVATE PROPERTY (1932) (theorizing that when shareholders are too dispersed, agency

control, while reminding us of the risks that are inherent in a commercial restructuring process that empowers a few stakeholders to make decisions that impact the investments of all others. Finally, it reignites the discourse on equity and fairness in the financial markets, and highlights the importance of a more transparent and equitable commercial restructuring process in carrying these principles through the entire life cycle of the firm.

This Article is organized as follows: Part II evaluates the traditional legal structures that have the potential to advance the interests of the debtor's shareholders in large commercial bankruptcies. Finding that these structures fail to offer adequate representation to non-insider common shareholders, Part III explores grassroots shareholder activism as a natural and spontaneous response to shareholders' collective action problem. Part III also constructs a more nuanced understanding of grassroots shareholder activism in large commercial bankruptcies by presenting the views of individual common shareholders themselves, with particular attention to their methods and motivations. Part IV explores various legal reforms that have the potential to provide formal representation to shareholders in Chapter 11 bankruptcy, thereby improving the fairness and efficiency of the commercial restructuring process. Part V concludes by reinforcing the argument that individual common shareholders must have a meaningful opportunity to participate in large commercial bankruptcies. Shareholders simply cannot protect their substantive rights without a collective voice in the proceedings and a seat at the bankruptcy negotiation table.

II. BACKGROUND: THE FAILURE OF TRADITIONAL LEGAL STRUCTURES TO PROMOTE SHAREHOLDERS' INTERESTS IN BANKRUPTCY

Whether within or outside of bankruptcy, shareholders of large, publicly traded corporations face overwhelming collective action obstacles.[37] For one thing, they tend to be widely dispersed[38] and possess divergent economic interests.[39] Moreover, their interests

problems arise whereby managers tend to advance their own self-interests). *See generally* Adolf A. Berle, *For Whom Corporate Managers are Trustees: A Note*, 45 HARV. L. REV. 1365 (1932) (further exploring these arguments). Berle's conception of the modern corporation is carefully reconsidered in 35 SEATTLE U. L. REV. 1009 (2012) (publishing the symposium articles from Berle III: Theory of the Firm, the Third Annual Symposium of the Seattle University School of Law's Adolf A. Berle, Jr., Center on Corporations, Law & Society).

37. *See* Kelli Alces, *The Equity Trustee*, 42 ARIZ. ST. L.J. 717, 735 (2010) (exploring the collective action obstacles faced by shareholders of large corporations, and proposing an "equity trustee" to better represent their interests); Stephen M. Bainbridge, *The Case for Limited Shareholder Rights*, 53 UCLA L. REV. 601, 616 (2006) (acknowledging the overwhelming collective action obstacles confronted by shareholders of large corporations); Margaret M. Blair & Lynn A. Stout, *A Team Production Theory of Corporate Law*, 85 VA. L. REV. 247, 312 (1999) (also noting the pronounced collective action obstacles faced by shareholders of large corporations). *See generally supra* note 13 (referencing collective action principles more broadly and with respect to corporate shareholders).

38. BERLE & MEANS, *supra* note 36, at 47–48. The phenomenon, along with the attendant collective action obstacles, are more recently observed in Lucian A. Bebchuk, *The Myth of the Shareholder Franchise*, 93 VA. L. REV. 675 (2007).

39. The deeply fractured nature of ownership in the modern corporation has led some scholars to believe that shareholders ought not to play a substantial role in governance. *See generally* Iman Anabtawi, *Some Skepticism About Increasing Shareholder Power*, 53 UCLA L. REV. 561 (2006) (arguing that increasing shareholder power will not benefit shareholders generally because dominant shareholders often have private interests that are in conflict with maximizing overall shareholder wealth); Bainbridge, *supra* note 37, at 632 (acknowledging the overwhelming collective action obstacles confronted by shareholders of large corporations).

may deviate from those of the corporation and its managers.[40] These challenges are only further amplified when a company faces financial difficulties. The following Subparts consider the limitations of the traditional legal structures that have the potential to advance the interests of shareholders of financially distressed firms, using examples from *Eastman Kodak* and other recent large commercial bankruptcies.

A. The Debtor's Management

The corporate debtor's management—and in particular, its board of directors—is the obvious starting place in any comprehensive review of the traditional legal structures that have the potential to advance shareholders' interests. This is because under U.S. corporate laws,[41] a board of directors manages the corporation.[42] While the board is responsible for approving major corporate decisions,[43] it typically delegates daily managerial functions to executive officers and advisors.[44]

Of course, a firm's managers may have their own divergent self-interests that cannot be reconciled with the corporation's best interests.[45] In recognition of the inherent potential conflicts,[46] courts adjudicating disputes of this sort typically opine that a solvent corporation's board and officers owe fiduciary duties first and foremost to the shareholders, as the firm's residual claimants (and thus the owners).[47] This means that managers are

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40. Berle, *supra* note 36 (exploring these and related agency problems). *See generally* Leonard I. Rotman, *Re-evaluating the Basis of Corporate Governance in the Post, Post-Enron Era*, *in* CORPORATE GOVERNANCE AFTER THE FINANCIAL CRISIS (P. M. Vasudev & Susan Watson eds., 2012) (exploring the disconnect between shareholders' interests and the corporation's interests).

41. Corporations are governed by the laws of the state in which they are incorporated. Outside of Delaware, most states model their corporation codes on some version of the Model Business Corporation Act (MBCA), a proposed uniform code drafted by the American Bar Association Section of Business Law, Committee on Corporate Laws. However, among public companies there is a persistent preference for Delaware as a state of incorporation. *See* Lucian Arye Bebchuk & Alma Cohen, *Firms' Decisions Where to Incorporate*, 46 J.L. & ECON. 383, 391 Table 2 (2002); Charles R. T. O'Kelley, *Delaware Corporation Law and Transaction Cost Engineering*, 34 GA. L. REV. 929, 933 (2000) (citing empirical evidence of this enduring preference). As a result, Delaware corporate law deserves special emphasis.

42. *See, e.g.*, DEL. CODE ANN. tit. 8, § 141 (2013) ("The business and affairs of every corporation organized under this chapter shall be managed by or under the direction of a board of directors"); MODEL BUS. CORP. ACT § 8.01 (2002); *see also* Cont'l Sec. Co. v. Belmont, 99 N.E. 138, 142 (N.Y. 1912) (articulating the classic view that corporate governance is vested in the board of directors).

43. DEL. CODE ANN. tit. 8, §§ 151–52, 251–66, 271–85 (2013); MODEL BUS. CORP. ACT § 8.01 (2002).

44. DEL. CODE ANN. tit. 8, § 142 (2013); MODEL BUS. CORP. ACT § 8.40, 8.41 (2002).

45. BERLE & MEANS, *supra* note 36, at 114; *see also* Michael C. Jensen & William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs & Ownership Structure*, 3 J. FIN. ECON. 305, 313 (1976) (noting the inherent conflict of interest between potentially opportunistic managers and shareholders).

46. *See* Robert Flannigan, *The Economics of Fiduciary Accountability*, 32 DEL. J. CORP. L. 393, 393 (2007) (fiduciary accountability promotes the "the utility of the conventional proscription on self-interest"); Andrei Shleifer & Robert W. Vishny, *A Survey of Corporate Governance*, 52 J. FIN. 737, 752 (1997) (corporate governance rules aim to prevent opportunistic behavior by self-interested managers).

47. *See, e.g.*, Koehler v. Black River Falls Iron Co., 67 U.S. 715, 720–21 (1862) ("[Corporate managers] hold a place of trust, and by accepting the trust are obliged to execute it with fidelity, not for their own benefit, but for the common benefit of the stockholders of the corporation."); Gantler v. Stephens, 965 A.2d 695, 708–09 (Del. 2009) ("[O]fficers of Delaware corporations, like directors, owe fiduciary duties of care and loyalty, and . . . the fiduciary duties of officers are the same as those of directors."). The rule is premised on the assumption that

expected to engage in business decisions that are intended to maximize the value of the corporation's common stock, even if this course of conduct fails to advance managers' self-interests or the interests of the firm's other constituents, such as preferred stockholders, creditors and employees.[48] Under most modern formulations of the corporate board's responsibilities, directors owe a duty of care, candor and confidence, and must work diligently on behalf of the corporation;[49] moreover, directors must resist conflicts of interests.[50] According to a leading corporate theoretical paradigm, fiduciary duties of this sort reduce the agency costs that arise when widely dispersed shareholders with profound collective action obstacles defer authority and control to managers who may otherwise be inclined to pursue their self-interests.[51] In essence, corporate law recognizes that the mechanisms of corporate governance offer imperfect representation and relies upon fiduciary principles to reduce the obvious risks to those who expose their capital investments to the ultimate decision-making powers of a board.[52]

Board fiduciary duties may shift in times of corporate financial distress. This is because when a corporation becomes insolvent, directors and officers are expected to

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shareholders are the residual claimants—and thus the owners—of the firm. *In re* Trados Inc. S'holder Litig., 73 A.3d 17, 40–41 (Del. Ch. 2013). ("To reiterate, the standard of conduct for directors requires that they strive in good faith and on an informed basis to maximize the value of the corporation for the benefit of its residual claimants, the ultimate beneficiaries of the firm's value . . . ."). However, this "shareholder primacy" theory of the firm has been called into question, most notably in Blair & Stout, *supra* note 37 (arguing that corporate boards possess a broad range of discretion that can be used to advance the interests of many corporate constituencies).

48. *See, e.g.*, Equity-Linked Investors, L.P., v. Adams, 705 A.2d 1040, 1042 (Del. Ch. 1997) (noting that a corporation's board of directors owes fiduciary duties to the common shareholders, and owes only contractual duties to its preferred stockholders. Also holding that "generally it will be the duty of the board, where discretionary judgment is to be exercised, to prefer the interests of common stock . . . to the interests created by the special rights, preferences, *etc.*, of preferred stock, where there is a conflict."); *see also* Katz v. Oak Indus. Inc., 508 A.2d 873, 882 (Del. Ch. 1986) (same, albeit with respect to bondholders rather than preferred stockholders).

49. The duty of care owed by a corporation's board of directors is generally understood to mean "act[ing] on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company." Smith v. Van Gorkom, 488 A.2d 858, 872–73 (Del. 1985), *overruled on other grounds by* Gantler v. Stephens, 965 A.2d 695 (Del. 2009). This means that directors must engage in substantial inquiry and/or seek expert advice. *Id.*

50. For instance, managers may not engage in "self-dealing." *See, e.g.*, Boston Children's Heart Found., Inc., v. Nadal-Ginard, 73 F.3d 429, 433–34 (1st Cir. 1996).

51. "Agency costs" include the costs of opportunism by managers with divergent self-interests, and the costs of establishing and maintaining effective controls to prevent opportunism. These costs have been extensively explored in the corporate literature. *See, e.g.*, Myron T. Steele, *The Moral Underpinnings of Delaware's Modern Corporate Fiduciary Duties*, 26 NOTRE DAME J.L. ETHICS & PUB. POL'Y 3, 14–19 (2012) (considering the relationship between corporate fiduciary duties and agency theories); Jensen & Meckling, *supra* note 45, at 305 (a foundational work exploring these concepts); *see also* Victor Brudney, *Corporate Governance, Agency Costs, and the Rhetoric of Contract*, 85 COLUM. L. REV. 1403, 1432–33 (1985) (exploring opportunistic behavior by firm managers). Of course, this agency view of the firm is not the only theoretical paradigm. The prominent "team production" theory of the firm suggests that the board exists to resolve high-level disputes about firm-specific investments made by all corporate constituents, including but not limited to shareholders. *See generally* Blair & Stout, *supra* note 37 (setting forth this theory of the firm). Under this approach, then, no legal support exists for privileging shareholders above other constituents.

52. *See generally supra* note 45 and sources cited therein (noting the inherent conflict of interest between potentially opportunistic managers and shareholders).

consider the best interests of the firm's creditors and strive to maximize the value of the company for *all* residual claimants, including creditors.[53] This shift is premised upon changing economic realities: creditors of an insolvent corporation bear a very real risk of nonpayment, such that they unwittingly become residual beneficiaries of any increase in value of the firm.

The problem, however, is that it is not always clear when a board's fiduciary obligations have been realigned in situations of corporate financial distress. This is because any such shift turns on the corporation's financial health, which can be difficult to discern in the case of a complex business enterprise.[54] To best approximate a corporation's financial condition for the purposes of identifying the beneficiaries of board fiduciary duties, corporate law generally[55] recognizes two tests for insolvency: balance sheet insolvency and cash flow insolvency.[56] The latter test examines the firm's ability to pay its debts as they come due,[57] while the former compares the value of the firm's assets to its liabilities.[58]

In practice, the realignment of traditional fiduciary duties to an expanded set of beneficiaries in the event of insolvency does not necessarily reduce the agency costs to shareholders *or* creditors. By grouping these investor classes together as co-beneficiaries of board fiduciary duties, the rule fails to take into account the inherent conflicts among these disparate stakeholders—particularly once the corporation enters bankruptcy.[59] For

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53. The principle is well-established in Delaware corporate law. *See, e.g.*, N. Am. Catholic Educ. Programming Found., Inc. v. Gheewalla, 930 A.2d 92, 103 (Del. 2007) (acknowledging that when a corporation becomes insolvent managers have a fiduciary duty to all residual claimants while holding that creditors of an insolvent corporation do not have a right to assert a claim for breach of fiduciary duty). *See also* Lynn M. LoPucki & William C. Whitford, *Corporate Governance in the Bankruptcy Reorganization of Large, Publicly Held Companies*, 141 U. PA. L. REV. 669, 709 (1993) (explaining that "management 'owes' fiduciary duties to both the creditors and the shareholders of an insolvent company, until their claims or interests are extinguished as part of the reorganization case").

54. Most large corporations use the accrual method of accounting, which requires considerable amounts of estimation and even speculation. *See* ASISH K. BHATTACHARYYA, ESSENTIALS OF FINANCIAL ACCOUNTING 647–48 (2011) (defining "accounting estimates" and "accrual convention").

55. As recently argued by attorneys for the prominent Delaware commercial law firm, Richard, Layton & Finger, Delaware courts apply these tests inconsistently. *See* Robert J. Steam, Jr. & Cory D. Kandestin, *Delaware's Solvency Test: What Is It and Does It Make Sense? A Comparison of Solvency Tests Under the Bankruptcy Code and Delaware Law*, 36 DEL. J. CORP. L. 165, 165–66 (2011).

56. *Id.* at 174–83 (describing the tests as articulated in Delaware corporate jurisprudence).

57. *See, e.g.*, Blackmore Partners, L.P. v. Link Energy L.L.C., No. Civ. A. 454-N, 2005 WL 2709639, at *3 (Del. Ch. 2005) (using both the cash flow test and the balance sheet test to analyze corporate solvency). Also referred to as "equitable insolvency," the cash flow test has been recommended by the World Bank where countries have chosen to include an insolvency requirement in their bankruptcy laws. *See, e.g.*, WORLD BANK, PRINCIPLES AND GUIDELINES FOR EFFECTIVE INSOLVENCY AND CREDITOR RIGHTS SYSTEMS ¶ 90 (2001) (arguing for a corporate solvency test which balances competing interests).

58. *See, e.g.*, Geyer v. Ingersoll Publ'ns Co., 621 A.2d 784, 789 (Del. Ch. 1992) (using the balance sheet test). This is also the test used for federal bankruptcy purposes. *See infra* note 132 (defining insolvency under the bankruptcy code).

59. Such conflicts are explored in Michelle M. Harner, *The Search for an Unbiased Fiduciary in Corporate Reorganizations*, 86 NOTRE DAME L. REV. 469 (2011) (outlining the conflicts among management, shareholders and creditors in bankruptcy); LoPucki & Whitford, *supra* note 53, at 709 (acknowledging that "the law of fiduciary duty does not provide a reliable way for either creditors or shareholders to check management when it

instance, in the typical bankruptcy reorganization, management's primary goal may be to preserve the company as a going concern and obtain confirmation of a Chapter 11 plan: a task that generally requires making concessions to some classes of claimants and interest holders at the ultimate expense of others.[60]

A corporation may file for Chapter 11 bankruptcy protection without necessarily meeting either or both insolvency tests. This is because, with the exception of municipal debtors, persons who seek federal bankruptcy protection are not required to be insolvent.[61] In these situations, shareholders are still the exclusive beneficiaries of managers' fiduciary duties under state corporate laws.[62] Bankruptcy law, by and through its broad mandate that the debtor take steps to maximize its value,[63] merely reinforces these fiduciary obligations.

Nonetheless, whether a firm is solvent or insolvent, shareholders typically fare poorly in Chapter 11 cases, for reasons that do not simply reflect economic realities.[64] For one thing, as drafters of the Bankruptcy Code[65] acknowledged, there is a "natural tendency of a debtor in distress to pacify large creditors, with whom the debtor would expect to do business, at the expense of small and scattered public investors."[66] For instance, early in Eastman Kodak Company's recent bankruptcy case, the debtor and its managers assumed

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acts in an otherwise appropriate manner on matters with regard to which the interests of creditors and shareholders conflict").

60. Over the years, policymakers, scholars and judges have disagreed as to whether debtors tend to favor creditors or shareholders. *See, e.g.*, *In re* Pilgrim's Pride Corp., 407 B.R. 211, 218 (Bankr. N.D.Tex. 2009) (noting that debtors tend to make concessions to creditors at the ultimate expense of shareholders); Raymond Nimmer, *Negotiated Bankruptcy Reorganization Plans: Absolute Priority and New Value Contributions*, 36 EMORY L.J. 1009, 1060 (1987) (asserting that shareholders have indirect influence over the debtor and its management, enabling them to bargain for excess returns); *see also infra* note 66 and accompanying text (describing the Bankruptcy Code drafters' view that debtors are more likely to align with creditors). In their influential empirical project, Professors LoPucki and Whitford found that in 43 large commercial cases, management's orientation was highly complex and also "clearly a function of the company's solvency. The managements of solvent companies never aligned with creditors, while the managements of insolvent companies did so frequently." LoPucki & Whitford, *supra* note 53, at 745. But it is important to note that in all five of the cases in their study in which management aligned with shareholders, an active shareholder owning a large block of stock also served as a board member. *Id.* at 746. Perhaps in light of this alternative explanation for managerial alignment with shareholders, the authors concluded that, in general, "creditors often exert considerable control over a reorganizing company." *Id.* at 713.

61. The Ninth Circuit recently reiterated this principle in *In re* Marshall III, 721 F.3d 1032, 1069 (9th Cir. 2013) (holding that Congress validly exercised constitutional power by allowing a debtor who is solvent to enter bankruptcy); *see also* Troy A. McKenzie, *Toward a Bankruptcy Model for Nonclass Aggregate Litigation*, 87 N.Y.U. L. REV. 960, 1019 n.230 (2012) (noting that only Chapter 9 Bankruptcy imposes a solvency requirement).

62. *Supra* note 47 and accompanying text.

63. 11 U.S.C. § 1107(a) (establishing that the debtor in possession has all the rights and obligations of a trustee); Official Comm. of Unsecured Creditors of Cybergenics Corp. v. Chinery, 330 F.3d 548, 573 (3d Cir. 2003) (noting the "trustee's fiduciary duty to maximize the value of the bankruptcy estate").

64. *See generally* Kelli A. Alces, *Enforcing Corporate Fiduciary Duties in Bankruptcy*, 56 U. KAN. L. REV. 83 (2007) (exploring the difficulties of applying state corporate fiduciary law in the federal bankruptcy context); LoPucki & Whitford, *supra* note 53, at 673 (detailing the complex ways in which managers control corporate restructurings, and acknowledging that "creditor and shareholder influence over management frequently prevents companies from maximizing their value").

65. All references herein to the Bankruptcy Code are to the Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549 (1978) (codified as amended at 11 U.S.C. §§ 101 et. seq.).

66. S. REP. NO. 95-989, at 5796 (1978).

an adversarial stance in response to shareholders' efforts to gain a seat at the negotiation table.[67] As a result, many shareholders came to believe that management had abandoned their interests entirely.[68] A similar criticism was leveled years earlier by shareholders of Northwest Airlines Corporation, who argued that "the central issue in this case . . . is that the Debtors have abandoned their public stockholders in all respects."[69]

Moreover, the modern commercial bankruptcy reorganization process under Chapter 11 privileges claimants with market power in the capital and securities markets, who are able to take control of the case and steer the restructuring towards an outcome that best advances their own interests.[70] The debtor's widely dispersed common shareholders are at a profound disadvantage unless they can find some way to counter this power. And yet, as the following Subpart explores, the modern commercial bankruptcy process under Chapter 11 does little to supplement corporate law when it comes to providing formal representation to the debtor's shareholders. Rather, bankruptcy law erects an even higher barrier against shareholder participation in negotiations.

B. *Official Committees to Represent Claimants in Bankruptcy*

Once a corporation files for bankruptcy protection, bankruptcy law, in addition to state corporate law, governs relations between and among the debtor's stakeholders. In a Chapter 11 case, the Bankruptcy Code authorizes the U.S. Trustee[71] to appoint one or more official committees to represent persons with an interest in the debtor's estate,[72] such as creditors and equity security holders.[73] An official equity committee is generally comprised of persons holding the "seven largest amounts of equity securities of the debtor of the kinds represented on such committee."[74] Members of the committee are expected to, among other things, retain professionals to represent the committee,[75] investigate the debtor's affairs, and assist with the preparation of a Chapter 11 plan.[76] Under bankruptcy law, those who serve on official committees owe fiduciary duties to the investors they represent.[77]

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67. *See, e.g.*, *infra* note 102 and source cited therein.

68. *See, e.g.*, Subzeroooo, *Shareholders' Interest Looked After by BOD...my a$$* (Sept. 5, 2013, 4:12 PM), http://kodak.boards.net/thread/6535/shareholders-interest-looked-after-bod (unequivocally expressing this sentiment on a shareholder message board).

69. Statement of Ad Hoc Committee Withdrawing Motion for Official Equity Comm. at 2, *In re* Northwest Airlines Corporation, Case No. 05-17930 (ALG), (Bankr. S.D.N.Y. Feb. 28, 2007), ECF No. 5086.

70. Dick, *supra* note 14, at 789.

71. By "U.S. Trustee," I mean the appropriate U.S. Trustee Office responsible for administering a bankruptcy case. *See, e.g.*, 28 U.S.C. § 586 (establishing 21 regional U.S. Trustee Offices).

72. The filing of a bankruptcy petition creates an estate that includes "all legal or equitable interests in property of the debtor." 11 U.S.C. § 541(a).

73. 11 U.S.C. § 1102.

74. 11 U.S.C. § 1102(b)(2). Such persons must also be "willing to serve." *Id.*

75. 11 U.S.C. § 1103(a).

76. 11 U.S.C. § 1103(c).

77. *See In re* Smart World Techs., LLC, 423 F.3d 166, 175 n.12 (2d Cir. 2005) ("[A] creditors' committee owes a fiduciary duty to the class it represents."); *In re* Johns-Manville Corp., 26 B.R. 919, 924 (Bankr. S.D.N.Y. 1983) ("[A] holder of a claim or an equity interest who serves on a committee undertakes to act in a fiduciary capacity on behalf of the members of the class he represents.").

In Chapter 11's legislative history, Congress explained that official committees were designed to be "the primary negotiating bodies for the formulation of the plan of reorganization."[78] In most large and complex restructuring cases, having an official committee means that a certain class of stakeholders is invited to the negotiation table. When equity owners in particular are invited to the negotiation table, it is highly likely that shareholders will settle their claims. As Professors Lynn LoPucki and William Whitford's comprehensive empirical study of commercial bankruptcies under Chapter 11 revealed, plan proponents successfully negotiated with the official equity committee—meaning that they gained the committee's consensus to the Chapter 11 plan—in 91% of observed cases in which such a committee existed.[79]

For these reasons, Eastman Kodak Company shareholders believed that having an official equity committee would enable them to effectively organize and participate in the company's restructuring. When the company entered bankruptcy in January 2012, it had approximately 270 million shares of common stock issued and outstanding.[80] Like any widely held public company, individual retail and retirement investors owned many of the debtor's common equity shares. But despite the magnitude of the common shareholder class, the U.S. Trustee appointed only a creditors' committee.[81] This is because, while the U.S. Trustee is obligated to appoint an official committee of unsecured creditors in Chapter 11 cases,[82] the appointment of an official committee of equity security holders is discretionary under the Bankruptcy Code.[83]

In the weeks following Eastman Kodak's bankruptcy petition, a group of common shareholders—mostly hedge funds—sent letters to the U.S. Trustee requesting the appointment of an official equity committee.[84] Following the U.S. Trustee's denial in February 2012,[85] these large and relatively powerful shareholders next filed a motion asking that the presiding U.S. Bankruptcy Court for the Southern District of New York

78. H.R. REP. NO. 95-595, at 401 (1977).

79. Lynn M. LoPucki & William C. Whitford, *Bargaining Over Equity's Share in the Bankruptcy Reorganization of Large, Publicly Held Companies*, 139 U. PA. L. REV. 125, 138 (1990).

80. Voluntary Petition of Eastman Kodak Co., at 4, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. Jan. 19, 2012), ECF No. 1.

81. Appointment of Official Comm. of Unsecured Creditors, at 1, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. Jan. 25, 2012), ECF No. 115.

82. 11 U.S.C. § 1102(a)(1) ("[T]he United States trustee shall appoint a committee of creditors holding unsecured claims.").

83. *Id.* ("[T]he United States trustee . . . may appoint additional committees of creditors or of equity security holders as the United States trustee deems appropriate."). *See In re* McLean Indus., Inc., 70 B.R. 852, 856 (Bankr. S.D.N.Y. 1987) (stating that U.S. Trustees have broad discretion to appoint additional official committees).

84. *See* Kodak S'holders' Joint Motion for Order Directing the Appointment of an Official Comm. of Equity Sec. Holders, at 2, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. Mar. 9, 2012), ECF No. 545 [hereinafter Kodak S'holders' Joint Motion for Order] (stating that shareholder value entitlements warranted the appointment of an official equity committee); *see also* Letter to Judge re: Joint Motion to Appoint Committee of Equity Security Holders, at 1, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. Mar. 30, 2012), ECF No. 789 [hereinafter Letter to Judge] (stating that an individual common shareholder lends his support to the joint motion).

85. *See supra* note 84 and sources cited therein (evidencing that while the shareholders claimed that they lacked adequate representation in the case, the U.S. Trustee ultimately denied the shareholders' request to appoint an official equity committee).

review the matter *de novo*.[86] In particular, moving shareholders argued that the evidence strongly suggested that the company was solvent and therefore had significant equity value to protect, and that shareholders were without adequate representation in the case because, among other things, the company's management had "already evidenced its disinclination towards shareholders by . . . vigorously opposing the appointment of an official equity committee [and] predicating that opposition on a premature and unstudied conclusion that equity is—and forever will be—out-of-the-money."[87] Consequently, moving shareholders asked the court to order the U.S. Trustee to form an official equity committee.[88] Although such relief is permissible under the Bankruptcy Code,[89] the court denied the motion in June 2012 on the grounds that shareholders were adequately represented by the debtor's management and by the creditor's committee, both of which were theoretically tasked with the duty of maximizing the value of the bankruptcy estate for the benefit of all stakeholders, including shareholders.[90]

Denied a seat at the negotiation table and effectively relegated to the sidelines, shareholders—large and small—anxiously awaited a draft Chapter 11 plan. Over a year later, the debtor and its management unveiled a proposed Chapter 11 plan reflecting negotiated settlements among the company and its creditors.[91] Upon reviewing the draft plan, shareholders discovered that they would receive no distributions and that their equity interests would be cancelled.[92] While this restructuring outcome would be consistent with bankruptcy's distributional norms and state corporate law if the debtor was in fact insolvent, the debtor never actually proved that it was insolvent.[93] Shareholders believed the company was vastly undervalued, as its financial disclosures relied upon book, rather than fair market, value.[94] In fact, the company's own plan-related disclosures touted its "cash-generative businesses" and "excellent positioning to achieve volume and profitability gains in the growth markets."[95] Because the draft Chapter 11 plan gave certain of the company's creditors all of the equity in the reorganized company,[96] some

86. Kodak S'holders' Joint Motion for Order, *supra* note 84, at 4–5.

87. *Id.* at 19.

88. *Id.* at 22.

89. 11 U.S.C. § 1102(a)(2).

90. *In re* Eastman Kodak Co., No. 12-10202, 2012 WL 2501071, at *2 (Bankr. S.D.N.Y. June 28, 2012).

91. *See* Joint Chapter 11 Plan of Reorganization of Eastman Kodak Co. and its Debtor Affiliates, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. Apr. 30, 2013), ECF No. 3650 [hereinafter Joint Chapter 11 Plan] (setting forth the debtor's draft plan of reorganization).

92. *See id.* at 29 (providing that "[n]o Holder of an Equity Interest in Kodak shall receive any Distributions on account of its Equity Interest").

93. Shareholder Greg Armstrong raised this and related criticisms in his objection. Objection by Greg Armstrong, S'holder (Pro Se) to the First Amended Joint Chapter 11 Plan of Reorganization of Eastman Kodak Co. and its Debtor Affiliates, at 9, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. Aug. 12, 2013), ECF No. 4737.

94. *See infra* notes 136 and 141 and accompanying text.

95. First Amended Disclosure Statement for Debtors' First Amended Joint Plan of Reorganization Under Chapter 11 of the Bankr. Code, at 2, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. June 24, 2013), ECF No. 4143.

96. On the treatment of creditors under the proposed plan, see Joint Chapter 11 Plan, *supra* note 91, at 26–29. Shareholders believed the company was vastly undervalued because the debtor had disclosed only book values, which did not reflect present economic realities. *See infra* note 136 and accompanying text. The ability of

shareholders believed that these creditors stood to profit from the restructuring at their expense. In essence, the draft plan underscored the true costs to shareholders of their disenfranchisement throughout the case. And so, shareholders once again mobilized. But although hedge funds initially advocated on behalf of shareholder interests, this time it would be individual common shareholders carrying the torch—using Internet message boards[97] and online digital libraries[98] to develop a defensive strategy and circulate documents.

Throughout the spring and summer of 2013, individual shareholders engaged in a grassroots effort to reignite the hedge funds' earlier petition for an official equity committee. When the U.S. Trustee once again declined this request in June 2013,[99] shareholders entered dozens of letters and motions on the docket,[100] asking the court to use its broad powers to order the U.S. Trustee to appoint an official equity committee.[101] The debtor and its management,[102] the U.S. Trustee,[103] and the official creditors' committee formally opposed these requests.[104]

Following an August 2013 hearing,[105] the court once again declined to order the U.S. Trustee to appoint an official equity committee.[106] Refusing to accept the shareholders' evidence of the debtor's potential solvency,[107] the court declined to even acknowledge the

management and senior creditors to use Chapter 11 to extract excess returns in the form of equity security interests in the reorganized debtor is detailed in Michael T. Roberts, *The Bankruptcy Discount: Profiting at the Expense of Others in Chapter 11*, 21 AM. BANKR. INST. L. REV. 157 (2013).

97. KODAK SHAREHOLDERS.COM, http://kodak.boards.net/ (last visited Sept. 11, 2014) (showing the forum shareholders primarily used).

98. For instance, a Scribd.com user "stockboardguy" established a digital online library of over 100 documents pertaining to the case. *See* SCRIBD, http://www.scribd.com/stockboardguy/documents (last visited Sept. 11, 2014).

99. Objection of the United States Trustee to Shareholders' Motion for an Order Approving the Appointment of an Official Equity Comm., at 7, *In re* Eastman Kodak Co., Case No. 12–10202 (ALG) (Bankr. S.D.N.Y. Jul. 29, 2013), ECF No. 4468 [hereinafter Objection of the United States Trustee] (referencing a letter dated June 4, 2013 from Tracy Hope Davis, U.S. Trustee, to each of the requesting pro se shareholders).

100. *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. 2013) (evidencing such filings on the case docket).

101. *See, e.g.*, S'holders' Motion for an Order Approving the Appointment of an Official Equity Comm., *In re* Eastman Kodak Co., Case No. 12-10202 (ALG), (Bankr. S.D.N.Y. July 9, 2013), ECF No. 4249 (motion from shareholder requesting the court's appointment of an official equity committee); Objection of the United States Trustee, *supra* note 99, at 7 (discussing letters to the U.S. Trustee urging the formation of an official equity committee).

102. Debtors' Objection to S'holders' Motion for an Order Approving the Appointment of an Official Equity Comm. at 1, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG), (Bankr. S.D.N.Y. July 31, 2013), ECF No. 4503.

103. Objection of the U.S. Trustee to S'holders' Motion for an Order Approving the Appointment of an Official Equity Comm. at 1, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. July 29, 2013), ECF No. 4468.

104. Objection of Official Committee of Unsecured Creditors to Motion for Appointment of Official Committee of Equity Security Holders, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG), (Bankr. S.D.N.Y. July 31, 2013), ECF No. 4507.

105. Transcript of Hearing, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. Aug. 5, 2013) (on file with the author).

106. *In re* Eastman Kodak Co., No. 12-10202, 2013 WL 4413300, at *7 (Bankr. S.D.N.Y. Aug. 15, 2013).

107. *Id.*

need for formal equity representation. In closing remarks, the court seemed to characterize these shareholders as mere sore losers: "The Shareholders who have commenced or have joined in the current motion are apparently convinced that it cannot be possible that the company in which they invested has fallen so far that there is so little value for unsecured creditors and no value at all for shareholders."[108]

In essence, Eastman Kodak Company shareholders were up against a prevailing view that shareholders ought to be presumptively excluded from the negotiation table in Chapter 11 cases, as official equity committees are often unnecessary and might even be dangerously inefficient.[109] Professors LoPucki and Whitford's empirical work in the early 1990s partially bolstered this view.[110] The authors documented how equity committees negotiate for shareholder distributions even when they apparently have no legal right to share in the proceeds of the estate, as determined by the authors' calculation of property distributions made or to be made as of the date of plan confirmation.[111] Although the authors acknowledged that such distributions are in many ways the natural byproducts of a restructuring process that encourages negotiated settlements,[112] they were also highly critical of such "nuisance" settlements.[113] In an effort to improve the commercial bankruptcy process, they recommended a "preemptive cram down" to narrow the parties to a Chapter 11 proceeding.[114] Under their proposal, the bankruptcy court would, after notice and a valuation hearing, "extinguish[] the interests of the shareholders of clearly insolvent debtors. The purpose [would be] to prevent shareholders who have no plausible claim to share in the distribution under the absolute priority rule from disrupting the reorganization process in the hopes of obtaining such a share through negotiations."[115] The proposal sought to advance the common goals of controlling costs and reducing delays in

108. *Id.* at *3.

109. Courts have expressed skepticism towards official equity committees, questioning not only their economic utility but also the genuineness of their motives. *See In re* Kalvar Microfilm, Inc., 195 B.R. 599, 601 (Bankr. D. Del. 1996) ("The late timing of the motion ties into the only remaining purpose of an equity committee in this case, which would be to object to confirmation, and litigate the valuation issue. The aforementioned costs associated with the formation of an equity committee cannot be justified in light of this purpose."); *In re* Heck's, Inc., 112 B.R. 775, 803–04 (Bankr. S.D.W.Va. 1990) (accusing an official equity committee (and its retained professionals) of engaging in inefficient conduct during the course of the Chapter 11 case), *aff'd in part and rev'd in part by In re* Heck's Properties, Inc., 151 B.R. 739 (S.D.W.Va. 1992); *In re* Emons Indus., Inc., 50 B.R. 692, 694 (Bankr. S.D.N.Y. 1985) ("Not every case with public shareholders warrants an equity committee. Nor is it clear that when a committee is appointed but is unsuccessful in obtaining any benefit for shareholders under a plan that creditors through the allowance of an expense of administration should be obliged to bear the burden of the futile effort.").

110. The authors' series of articles included LoPucki & Whitford, *supra* note 53; LoPucki & Whitford, *supra* note 79; LoPucki & Whitford, *infra* note 113.

111. *See* LoPucki & Whitford, *supra* note 79, at 143–58 (discussing why equity holders share in the distributions).

112. LoPucki and Whitford acknowledge the importance of equity security committees in providing representation for shareholders, and also note that the distributions to shareholders are reflective of a system that encourages negotiated settlement rather than judicial edict in strict accordance with absolute priority. *See id.* at 190–94.

113. The authors clearly articulate their negative sentiments towards these distributions in Lynn M. LoPucki & William C. Whitford, *Preemptive Cram Down*, 65 AMER. BANKR. L.J. 625, 625 (1991).

114. LoPucki & Whitford, *supra* note 79, at 187–89; LoPucki & Whitford, *supra* note 113, at 625.

115. LoPucki & Whitford, *supra* note 113 at 625.

large commercial bankruptcy cases,[116] erring on the side of protecting creditors from further deterioration of the bankruptcy estate.[117] But it is important to note that for Professors LoPucki and Whitford, the debtor's solvency was pivotal to the decision whether to exclude shareholders: in their view, only those interest holders who are "clearly under water . . . [with] no reasonable probability that they will cease to be under water by confirmation"[118] should be subject to the preemptive cram down.[119] In cases of solvent, marginally solvent—or even *potentially* solvent debtors—equity owners presumably had an important role to play in bankruptcy negotiations. In their view, the proposal was "directed at a narrow range of cases."[120]

Although the proposal was never codified, if the decisions of the U.S. Trustee and the bankruptcy court in *Eastman Kodak* are any indication, common shareholders in modern commercial bankruptcy cases are presumptively excluded from the negotiation table and, as a result, preemptively crammed down in most cases. This is because a recent jurisprudential shift in bankruptcy law has further contributed to shareholder disenfranchisement in large commercial reorganizations. Although the Bankruptcy Code is silent as to the facts and circumstances that the U.S. Trustee ought to consider in handling shareholder requests to appoint an official equity committee, the question has spawned a complex body of judicial doctrine that is inconsistently applied by courts. Through this murky jurisprudence, courts have attempted to balance the statutory right of equity security holders to the appointment of a committee where "necessary" to achieve "adequate representation,"[121] with the much broader goal of an efficient and cost-effective bankruptcy process. Costs are a concern because, as the U.S. Bankruptcy Court for the Southern District of New York explained, official committee appointments are "closely followed by applications to retain attorneys and accountants,"[122] with such costs generally

116. On costs, *see infra* notes 122–123 and accompanying text. Judicial sensitivity to costs in Chapter 11 is more broadly considered in Melissa B. Jacoby & Edward J. Janger, *Ice Cube Bonds: Allocating the Price of Process in Chapter 11 Bankruptcy*, 123 YALE L.J. 862 (2014).

117. For instance, courts have expressed a need to control all types of administrative expenses in bankruptcy proceedings. The Eleventh Circuit articulated the view thusly: "Despite the expansiveness with which the administrative expense category may be treated, such judicial construction is limited by the countervailing doctrine that section 503 priorities should be narrowly construed in order to maximize the value of the estate preserved for the benefit of all creditors." Varsity Carpet Servs., Inc. v. Richardson (*In re* Colortex Indus., Inc.), 19 F.3d 1371, 1377 (11th Cir. 1994) (citing Otte v. U.S., 419 U.S. 43, 53 (1974)).

118. LoPucki & Whitford, *supra* note 113, at 628 (articulating this insolvency threshold).

119. Professor LoPucki reaffirms this view in a subsequent work. Lynn M. LoPucki, *The Trouble With Chapter 11*, 1993 WIS. L. REV. 729, 755–56 (1993) ("We think the elimination from the bargaining process of parties who have no legal right to share in the distribution can eliminate a good deal of unnecessary threats, litigation, posturing and negotiating.").

120. LoPucki & Whitford, *supra* note 113, at 647.

121. 11 U.S.C. § 1102(a)(2). Like many pivotal concepts in bankruptcy law, the phrase "adequate representation" is not defined in the Bankruptcy Code.

122. *In re* Saxon Indus. Inc., 39 B.R. 945, 947 (Bankr. S.D.N.Y. 1984).

borne by the debtor's estate.[123] Similarly, there are less tangible burdens associated with committee formation, such as delays and interruptions in the bankruptcy process.[124]

A multi-factor analysis has emerged, with courts generally considering the following: the number of shareholders;[125] the case's complexity, as indicated by the debtor's capital structure;[126] the case docket's magnitude or the contested nature of Chapter 11 plan negotiations;[127] whether the tangible and intangible costs to the estate outweigh any potential gains to shareholders from adequate representation;[128] and whether the proceeding already adequately protects shareholder interests.[129] Although no one factor is intended to be dispositive,[130] courts typically focus the analysis on the debtor's solvency; in other words, most judges are only willing to expose the bankruptcy estate to the costs of an official equity committee when there is clearly equity to protect.[131]

But at or near the commencement of a case, it may be difficult to obtain a full and complete picture of the debtor's financial condition. Although the Bankruptcy Code mandates use of the ostensibly detached and objective balance sheet test to determine whether a debtor is insolvent,[132] the U.S. Trustee typically relies upon the debtor's own financial disclosures in exercising its discretion to appoint an official equity committee.[133] But financial disclosures that rely upon generally accepted accounting principles

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123. 11 U.S.C. § 503. Under subsection (b)(2), professionals retained by an official committee are entitled to administrative priority for payment of fees and expenses. Other professionals may be paid "reasonable compensation" under subsection (b)(4) only if the services make a substantial contribution to the bankruptcy case.

124. *See, e.g.*, Albero v. Johns-Manville Corp., 68 B.R. 155, 160 (Bankr. S.D.N.Y. 1986) (mentioning intangible costs).

125. *See, e.g.*, Thomas Henry Coleman & David E. Woodruff, *Looking Out for Shareholders: The Role of the Equity Committee in Chapter 11 Reorganization Cases of Large, Publicly Held Companies*, 68 AM. BANKR. L.J. 295, 298 (1994) (summarizing courts' consideration of this factor).

126. *See, e.g., In re* Edison Bros. Stores, Inc., No. 95-13554, 1996 WL 534853, at *2 (D.Del. Sept. 17, 1996) (considering the debtor's capital structure as evidence of the complexity of the case).

127. *See, e.g., In re* Wang Labs., Inc., 149 B.R. 1, 3 (Bankr. D. Mass. 1992) (evaluating the necessity of an official equity committee).

128. *See, e.g., In re* Public Serv. Co. of N.H., 116 B.R. 344, 345 (Bankr. D. N.H. 1990) (balancing the interests of shareholders against the burden of additional costs).

129. *See, e.g., In re* Exide, 2002 U.S. Dist. LEXIS 27210, at *4 (D.Del. Dec. 23, 2002) (holding that equity holders must be adequately represented); *Albero*, 68 B.R. at 159–61 (establishing the appropriate legal standard bankruptcy courts must follow in the use of their discretion to appoint an equity committee); *In re* Beker Indus., 55 B.R. 945, 947 (Bankr. S.D.N.Y. 1985) (ordering the appointment of official committees to represent equity and debenture holders.).

130. *In re* Edison Bros. Stores, Inc., No. 95-13554, 1996 WL 534853, at *3 (D.Del. Sept. 17, 1996) (stating that the factors "are simply guidelines for the courts to consider and every case must be judged on its own facts"); *see also In re* Residential Capital, LLC, 480 B.R. 550, 558 (Bankr. S.D.N.Y. 2012) (discussing seven factors that bankruptcy courts consider when deciding whether to appoint an official committee to ensure adequate representation for the moving party); *Matter of* Kalvar Microfilm, Inc., 195 B.R. 599, 600 (Bankr. Del. 1996) (stating the factors that courts consider when deciding whether to appoint additional committees).

131. For instance, the U.S. Bankruptcy Court for the Southern District of New York referred to the debtor's solvency as the "threshold issue." *In re* Ampex Corp., No. 08-11094, 2008 WL 2051128, at *1 (Bankr. S.D.N.Y. May 14, 2008).

132. Under the Bankruptcy Code, a company is insolvent when "the sum of such entity's debts is greater than all of such entity's property, at a fair valuation." 11 U.S.C. § 101(32)(A).

133. The U.S. Trustee may conduct an independent valuation by, among other things, reviewing the debtor's first-day filings and associated disclosures, as well as its most recent 8-K and 10-K filings.

(GAAP),[134] as they often do, may not give an accurate picture of the debtor's true economic condition.[135] For example, as numerous Eastman Kodak Company shareholders observed, the debtor's Chapter 11 plan-related financial disclosures recorded properties at cost, net of accumulated depreciation,[136] rather than at their potentially much higher fair market value. Similarly, certain corporate assets retain or lose value depending upon the nature of the restructuring ultimately pursued; for instance, to the extent the debtor possesses valuable tax attributes, its reorganization value may be much higher than its liquidation value.[137] Moreover, the court may subordinate or recharacterize certain liabilities as equity during the course of the bankruptcy case,[138] thereby dramatically altering the debtor's financial picture. Finally, the debtor or its stakeholders can easily manipulate financial data;[139] the risk is particularly high with respect to court-mandated bankruptcy disclosure forms, which do not fully take into account the complexity of modern commercial assets and liabilities.[140] Perhaps in recognition of these and similar issues, the debtor's financial disclosures in *Eastman Kodak* were replete with caveats that the data may be incomplete, inaccurate or misleading.[141] Shareholders raised these and

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134. Generally Accepted Accounting Principles are uniform standards of, and guidelines to, financial accounting and reporting. The Financial Accounting Standards Board and the Governmental Accounting Standards Board are authorized by the U.S. Securities & Exchange Commission to establish these principles. *Frequently Asked Questions*, AM. INST. OF CERTIFIED PUB. ACCOUNTANTS, http://www.aicpa.org/About/FAQs/Pages/FAQs.aspx (last visited Sept. 16, 2014).

135. *See, e.g.*, *In re* Sierra Steel, Inc. v. Totten Tubes Inc., 96 B.R. 275, 278 (B.A.P. 9th Cir. 1989) (holding that there is no evidence that GAAP accurately determines insolvency); *In re* Wang Labs, Inc., 149 B.R. 1 (Bankr. D.Mass 1992) (holding that the appointment of an official equity committee was necessary).

136. *See, e.g.*, Objection by Greg Armstrong, S'holder (Pro Se) to the First Amended Joint Chapter 11 Plan of Reorganization of Eastman Kodak Co. and its Debtor Affiliates, at 12–15, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. Aug. 12, 2013), ECF No. 4737 (making objections to the methods relied upon by the court to value Eastman Kodak's assets). The debtor principally calculated depreciation expense using the straight-line method over the assets' estimated useful lives, which are typically ten to 40 years for buildings, and three to 20 years for equipment.

137. *See* Dick, *supra* note 28, at 2273 (explaining that valuable tax attributes may be a unique asset that can be preserved in a Chapter 11 bankruptcy, and directed to preferred stakeholders).

138. Bankruptcy courts may subordinate claims on equitable grounds. Pepper v. Linton, 308 U.S. 295, 305 (1939); *see also* 11 U.S.C. § 510(c) (permitting the bankruptcy court to subordinate, on equitable grounds, all or part of a creditor's allowable claim).

139. For a lively account of the myriad possibilities, see generally HOWARD SCHILIT, FINANCIAL SHENANIGANS: HOW TO DETECT ACCOUNTING GIMMICKS & FRAUD IN FINANCIAL REPORTS (2010).

140. *See* Dick, *supra* note 28, at 2304 (providing the example that, "the omission of tax attributes from a debtor's preliminary asset disclosures leads to information asymmetries as to the nature and extent of what may be the debtor's most sizable asset").

141 Schedules of Assets and Liabilities for Eastman Kodak Company, at *3-4, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. Apr. 14, 2012), ECF No. 887 (providing global limitations and disclaimers with respect to the debtor's financial disclosures). For instance, the disclosure statement warns that "inadvertent errors or omissions may have occurred" and that "there can be no assurance that these [financial disclosures] are complete." *Id.* at *3. Under the heading "Valuation," the disclosure statement provides, "It would be prohibitively expensive, unduly burdensome, and an inefficient use of estate assets for the Debtors to obtain current market valuations of all of their assets. Accordingly . . . net book values as of December 31, 2011 are reflected." *Id.* at *4.

related arguments in their efforts to demonstrate that the debtor was not necessarily insolvent.[142]

Under an earlier line of cases, Eastman Kodak Company's shareholders would have likely received a favorable response to their requests for an official equity committee. This is because the dominant legal standard for appointment of an official equity committee was, for many years, much more lenient toward shareholders, requiring only a limited investigation of the debtor's solvency.[143] Precisely because of the vulnerable position the debtor's equity security holders occupied, drafters of the Bankruptcy Code desired to extend generous representation rights. For instance, legislative history reveals that Congress believed it was "essential for [public investors] to have legislative assurance that their interests will be protected," and that "[s]uch assurance should not be left to a plan negotiated by a debtor in distress and senior or institutional creditors who will have their own best interest to look after."[144] Recognizing the unique collective action obstacles faced by shareholders, the drafters hoped that the appointment of an official equity committee would counteract the tendency for debtors to appease creditors at the ultimate expense of shareholders.[145] These protections were viewed as especially necessary during bankruptcy, as reorganization proceedings are "literally the last clear chance to conserve for [shareholders] values that corporate financial distress or insolvency have placed in jeopardy."[146]

Accordingly, under the early standard, the debtor and/or its creditors had the burden of proving that shareholders ought to be excluded from the negotiation table. The U.S. Trustee was expected to affirmatively respond to shareholder requests to appoint an official equity committee except where the debtor appeared to be "hopelessly insolvent."[147] Cases applying this standard frequently noted that shareholders did not need to be guaranteed a distribution. Rather, shareholders need only make a showing that there is *potential* equity value such that they are not necessarily "out of the money."[148] For instance, as the U.S. Bankruptcy Court for the District of Massachusetts explained, the costs of equity representation are justified where the debtor is even "marginally solvent."[149] Some early decisions even reasoned that the debtor's demonstrated insolvency is not a bar to the appointment of an equity committee.[150] Disregarding economic efficiency arguments entirely and focusing instead on procedural fairness, the U.S. Bankruptcy Court for the Northern District of Ohio went so far as to note that the debtor's insolvency was altogether "irrelevant" to the analysis.[151] Even the U.S. Bankruptcy Court for the Southern District

142. *See generally supra* note 101 and sources cited therein (giving examples of shareholders' motions).

143. *See infra* notes 147 through 152 and accompanying text (listing cases that apply the more lenient legal standard).

144. S. REP. NO. 95-989, at 5796 (1978).

145. *Id.*

146. S. REP. NO. 95-989, at 10 (1978) *reprinted in* 1978 U.S.C.C.A.N. 5787, 5790.

147. The language was initially used in *In re* Emons Indus., Inc., 50 B.R. 692, 694 (Bankr. S.D.N.Y. 1985).

148. *In re* Mansfield Ferrous Castings, Inc., 96 B.R. 779, 781 (Bankr. N.D. Ohio 1988).

149. *In re* Wang Labs., Inc., 149 B.R. 1, 3 (Bankr. E.D. Mass. 1992).

150. *See In re Mansfield Ferrous Castings*, 96 B.R. at 781 (stating that the court will not look exclusively to the debtor's solvency); *In re Emons Indus.*, 50 B.R. at 694 (explaining that equity security holders could have a different view on the issue of insolvency).

151. *In re* White Motor Credit Corp., 27 B.R. 554, 558 (N.D. Ohio 1982).

of New York acknowledged in a 1987 ruling that "costs alone cannot and should not deprive public debt and security holders of representation."[152]

Professors LoPucki and Whitford's preemptive cram down proposal[153] fits nicely under a generous standard of this sort; by foreclosing the rights of interest holders in cases of clear insolvency, it serves as a check on a system that otherwise facilitates shareholder participation. At the time the authors issued their recommendation, bankruptcy process was much more inclusive of shareholders. In fact, by the mid-1990s, it had become much more common to see official equity committees in Chapter 11 cases involving large, publicly traded companies.[154] The trend picked up more steam in the early 2000s, leading several industry commentators to remark that the "appointment of a formal equity committee appears to have recently taken the US [sic] bankruptcy world by storm."[155] However, unbeknownst to these commentators at the time they made this remark, a jurisprudential shift had already begun to erode the legal foundation for the appointment of official equity committees in most cases.

As bankruptcy's common law evolved, the legal standard for the appointment of an official equity committee has become much less flexible to shareholder needs, and a new, largely unsupported alternative rule has taken root in the jurisdictions most likely to hear large commercial bankruptcies.[156] As in *Eastman Kodak*, courts applying the newer standard emphasize economic efficiency over procedural fairness, placing a high burden of proof on shareholders who seek the appointment of an official committee.[157] Under this approach, shareholders must demonstrate that there is a substantial likelihood that shareholders will receive a meaningful distribution in the Chapter 11 case under a strict application of the absolute priority rule.[158] In other words, it is not enough for shareholders to argue that the debtor is not hopelessly insolvent; rather, those requesting an official equity committee must show that there is in fact sufficient residual value to provide a distribution to equity security holders, even after all other claims and expenses are paid.[159] The standard effectively requires the court to ensure that shareholders, not creditors, will bear the economic burdens of forming an official equity committee.[160] This new standard

152. *In re* Mclean Indus., 70 B.R. 852, 860 (Bankr. S.D.N.Y. 1987).

153. *See supra* notes 114–120 (describing the authors' proposal).

154. *See* Thomas Henry Coleman & David E. Woodruff, *Looking Out for Shareholders: The Role of the Equity Committee in Chapter 11 Reorganization Cases of Large, Publicly Held Companies*, 68 AM. BANKR. L.J. 295, 295–96 (1994) (examining the then emergent trend of official equity committees in large commercial bankruptcies).

155. Bob Rajan & Brett Harrison, *The New Wave of Equity Committees in Bankruptcy: What Are They and Are They Here to Stay?*, 10 INT'L CORP. RESCUE 1, 1 (2006).

156. *See infra* notes 158–167 and accompanying text (including examples of cases in jurisdictions applying the referred alternative rule).

157. *See infra* note 164 and accompanying text (explaining how the alternative standard requires shareholders to demonstrate a substantial likelihood of a meaningful distribution before allowing the formation of an official equity committee).

158. *In re* Williams Commc'ns Grp, Inc., 281 B.R. 216, 220 (Bankr. S.D.N.Y. 2002).

159. *In re* Nat'l R.V. Holdings, Inc., 390 B.R. 690, 696 (Bankr. C.D. Cal. 2008) (taking administrative costs explicitly into consideration).

160. *See infra* note 164 and accompanying text (explaining how the *Williams* standard requires shareholders to demonstrate a substantial likelihood of a meaningful distribution before allowing the formation of an official equity committee). The costs of official committees "are paid by the debtor corporation, effectively passing these

arguably arose out of dicta[161] in *In re Williams Communications Group, Inc.*, a 2002 opinion from the U.S. Bankruptcy Court for the Southern District of New York.[162] After devoting much of its analysis to the "hopelessly insolvent" standard and even reiterating that the U.S. Trustee and the court need not make an actual valuation finding,[163] the *Williams* court summarized its holding by noting that "an equity committee should not be appointed unless equity holders can establish . . . a 'substantial likelihood' of a 'meaningful distribution.'"[164] This language has been adopted by the U.S. Trustee and by the U.S. Bankruptcy Courts for the Southern District of New York and the District of Delaware,[165] which are the two most common venues for large corporate filings under Chapter 11.[166] For instance, in *Eastman Kodak*, the U.S. Trustee and the U.S. Bankruptcy Court for the Southern District of New York relied upon *Williams* to twice deny shareholders' requests to appoint an official equity committee.[167]

As noted above, the *Williams* decision effectively shifts the burden of proof, doing significant violence to the ability of shareholders to participate in Chapter 11 plan negotiations.[168] It not only presumptively excludes shareholders, but also essentially effectuates Professors LoPucki and Whitford's preemptive cram down, in substance if not in form.[169] Of course, shareholders remain parties to the case and can attempt to raise arguments on their own. But by making it so difficult for shareholders to organize and obtain formal representation in the case, the decision forecloses meaningful shareholder participation and makes it highly unlikely that they will be able to successfully advance

costs on to some or all of the persons who will share in distributions under the reorganization plan." LoPucki & Whitford, *supra* note 53, at 680. In this way, the *Williams* standard attempts to be responsive to the cost concerns cited *supra* note 109.

161. Heather Lennox et al., *Best Practices Report: Formation, Function, and Obligations of Equity Committees in Chapter 11*, 2013 ANN. SURV. BANKR. LAW 5, 9 (2013) ("The *Williams* court's 'substantial likelihood' standard was sui generis (the court cited to no authority in support of its announced standard) and perhaps even dicta (although the court proposed this standard, it arguably did not apply it).").

162. *In re Williams*, 281 B.R. at 220.

163. *Id.* at 221.

164. *Id.* at 223.

165. The "substantial likelihood of a meaningful distribution" standard was applied by bankruptcy courts in the following cases, among others: *In re* Spansion, Inc., 421 B.R. 151, 156 (Bankr. D. Del. 2009); *In re* Oneida Ltd., 56 Collier Bankr. Cas. 2d (MB) 261, 2006 WL 1288576, at *1, *2 (Bankr. S.D.N.Y. 2006); *In re* Nw. Corp., 2004 WL 1077913, at *1, *2 (Bankr. D. Del. 2004).

166. This strong jurisdictional preference is recently noted in Laura Napoli Coordes, *The Geography of Bankruptcy*, 68 VAND. L. REV. 2, 9 (2014). Forum-shopping in large commercial bankruptcy cases was also the subject of empirical analysis in Lynn M. LoPucki & William C. Whitford, *Venue Choice and Forum Shopping in the Bankruptcy Reorganization of Large, Publicly Held Companies*, 1991 WIS. L. REV. 11, 12 (1991) (finding evidence of forum shopping in a substantial number of observed cases, with New York City as the most commonly selected venue).

167. *In re* Eastman Kodak Co., 2012 WL 2501071, at *1 (Bankr. S.D.N.Y. 2012); *In re* Eastman Kodak Co., 2013 WL 4413300, at *1, *2 (Bankr. S.D.N.Y. 2013).

168. *See supra* note 164 and accompanying text (describing the standard that must be met for an official equity committee to be appointed).

169. *See supra* notes 114–120 (describing the authors' proposal).

arguments or negotiate to receive a distribution.[170] And it does so across the board, without any of the safeguards or limitations that the authors recommended.[171]

The decision and its progeny rely upon relatively thin economic analyses of corporate and bankruptcy law, whereby large commercial debtors are assumed to be rational, unitary actors that are capable of deliberate action to maximize their economic utility.[172] Such actors would not submit to an expensive and time consuming Chapter 11 case unless they were so hopelessly insolvent that they would be unable to continue as a going concern without the special protections bankruptcy affords. In this way, the decision privileges economic efficiency goals over procedural fairness, creating a deep disparity in access to the negotiation table and thereby virtually ensuring relatively early in the case that shareholders will not receive a distribution.

Indeed, the untested economic theories underlying these assumptions, and their ability to blind courts to the economic realities of a given case, are fully evidenced in *Williams*. There, the court cited, as evidence of the debtor's hopeless insolvency, the fact that over one-third of the company's unsecured creditors agreed to settle billions of dollars in claims in exchange for equity in the reorganized debtor.[173] The court explained, "[t]his is a telling agreement since the opportunity for unsecured creditors to receive cash or restructured debt, for even a portion of their claim, [as opposed to 'the highly uncertain value of common stock'] would almost certainly have been seized."[174] It seems the court viewed the debtor as a rational, unitary actor, capable of taking deliberate steps to maximize its own economic utility, such that it would only pursue Chapter 11 reorganization if it were driven by its hopeless insolvency. The court failed to consider other possible explanations: that the debtor may have been captured by dominant creditors, that the reorganized debtor's equity interests might simply have been worth more than the debtors' financial disclosures suggested, and that creditors were comfortable assuming risks associated with equity investments in order to enjoy the full upside potential. At the same time, even after acknowledging that the creditors intended to advance to the equity position, the court expressed confidence that the official creditors' committee would adequately represent the company's historic shareholders.[175] Evidencing a policy preference that is contrary to precedent and congressional intent, the *Williams* court concluded with a stern proclamation that "[t]he appointment of official equity committees should be the rare exception."[176]

Following *Williams*, the U.S. Trustee and the most influential bankruptcy courts consistently echo this heightened standard. They construe the jurisprudence to require only that the U.S. Trustee review the available financial data and determine whether there are sufficient "indicator[s] of insolvency" to warrant refusal to appoint an official equity

170. *See infra* note 213 and accompanying text (explaining how Chapter 11 privileges organizational actors).

171. For instance, the authors propose a hearing in which the moving party presents evidence regarding the debtor's valuation. LoPucki & Whitford, *supra* note 113, at 636–43 (explaining the proposed mechanism and the various safeguards and limitations).

172. This pervasive view is explored in Dick, *supra* note 14.

173. *In re* Williams Commc'ns Grp. Inc., 281 B.R. 216, 221 (Bankr. S.D.N.Y. 2002).

174. *Id.*

175. *Id.* at 222.

176. *Id.* at 223.

committee.[177] When applied in this manner, the *Williams* court's reminder that the judge need not conduct a full valuation analysis at this stage merely ensures that the debtor's own financial disclosures and valuations will be afforded great deference, without regard to the inherent limitations of these data sources. The U.S. Bankruptcy Court for the Southern District of New York decided that courts may assign "presumptive validity" to determinations made under GAAP,[178] thereby rendering it even more difficult for shareholders (or any other parties) to challenge the debtors' claims. Meanwhile, the U.S. Bankruptcy Court for the Southern District of New York has repeatedly stated that additional committees, including official equity committees, should not be appointed unless those requesting such committees meet their burden of proof.[179] In practice, therefore, for shareholders to persist in their demand for an official committee, they must put forth a full valuation case of their own, without any guarantee that the expenses will be borne by the bankruptcy estate, or that the court will even be receptive to their arguments.

Thus, the modern jurisprudence establishes a substantial barrier to entry for shareholders of corporate debtors in Chapter 11 who wish to gain a seat at the negotiation table, amounting to the functional equivalent of a preemptive cram down of equity owners. Moreover, for shareholders who endeavor to prove the debtor's solvency, the analysis is frustratingly circular. For instance, when Eastman Kodak Company's shareholders made their first attempt to obtain an official equity committee, the court declined to consider the shareholders' evidence of the debtors' solvency. It noted that "[a]ny potential benefit to conducting [a valuation trial] is outweighed by the considerable time and expense it would impose on Kodak at this stage of its reorganization."[180] But ironically, a valuation case is necessary for shareholders to even attempt to demonstrate that there is a substantial likelihood of a meaningful distribution to equity holders.

Furthermore, even where a court is receptive to shareholders' arguments concerning valuation, there are obvious information asymmetries[181] and transaction costs[182] that make it difficult for shareholders to present a compelling case.[183] What is more, a successful

177. *Id.*

178. *See, e.g., In re* Centennial Textiles, Inc., 220 B.R. 165, 174 (Bankr. S.D.N.Y. 1998) (stating that "the court is inclined to assign presumptive validity to the treatment of assets and liabilities according to GAAP").

179. *Id.*; *see also In re* Residential Capital, LLC, 480 B.R. 550, 561 (Bankr. S.D.N.Y. 2012) (stating that the moving parties did not meet their burden so the case is not appropriate for the appointment of a separate committee).

180. *In re* Eastman Kodak Co., No. 12-10202, 2012 WL 2501071, at *3 (Bankr. S.D.N.Y. June 28, 2012).

181. The problem of information asymmetries, which arise when one party to a transaction has more or better information than the other(s), is explored in Joseph E. Stiglitz, Nobel Prize Lecture: Information and the Change in the Paradigm in Economics (Dec. 8, 2001), *available at* http://nobelprize.org/nobel_prizes/economics/laureates/2001/stiglitz-lecture.pdf (detailing Stiglitz's contributions to the field). *See generally* Bruce C. Greenwald & Joseph E. Stiglitz, *Externalities in Economies with Imperfect Information and Incomplete Markets*, 101 Q. J. ECON. 229 (1986) (considering the role of the government in addressing market inefficiencies caused by information asymmetries); George A. Akerloff, *The Market for "Lemons": Quality Uncertainty and the Market Mechanism*, 84 Q. J. ECON 488 (1970) (exploring the effect of information asymmetries in the used car market).

182. *See generally* Oliver E. Williamson, *The Economics of Organization: The Transaction Cost Approach*, 87 AMER. J. SOC. 548 (1981) (describing the potential economic distortions caused by transaction costs generally).

183. Moreover, the *Williams* standard incorporates the absolute priority rule, which is typically applied in a way that fails to capture all potential sources of economic wealth in the debtor's estate. For instance, as I've

attempt to obtain an official equity committee essentially requires shareholders of large, publicly traded corporations to overcome their collective action obstacles outside of the traditional legal structures, such as through deliberate, grassroots organization. In *Eastman Kodak*, these challenges were especially pronounced. In their second attempt to obtain an official equity committee, shareholders realized that they would need to present a full valuation case, or at least cast sufficient doubt upon the valuation data provided by the debtor and its management.[184] They strategized for months, largely on public Internet message boards.[185] In dozens of letters to the court and to the U.S. Trustee they argued, among other things, that the debtor's plan-related financial disclosures were flawed in that they assigned zero value to the company's extensive real property, foreign subsidiaries and intellectual property holdings.[186] Similarly, they claimed that the debtor failed to disclose substantial anticipated revenues from intellectual property transactions,[187] and declined to adequately report the expected revenue from prospective joint ventures or the net present value of the potential future benefits associated with the company's multibillion dollar net operating losses.[188] Shareholders compiled and submitted extensive research to support these assertions, including reports prepared by two expert witnesses.[189]

The company's management not only objected to the shareholders' motion,[190] but also filed *Daubert*[191] motions in limine to exclude most of the documentary evidence and

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argued elsewhere, the standard declines to take into consideration the full value potential of certain intangible assets—such as the debtor's tax attributes—because these assets would not be distributed to claimants in a liquidation. Dick, *supra* note 28, at 2273.

184. *See infra* notes 186–89.

185. *See, e.g.*, busted1964, *Balance Sheet March 31, 2013*, KODAK BOARD (May 5, 2013, 7:47 AM), http://kodak.boards.net/thread/5208/balance-sheet-march-31-2013 (reflecting upon the company's publicly disclosed financial data); bk25, *Valuation of Kodak/Uni-Pixel Partnership by Kodak Shareholders*, KODAK BOARD (May 3, 2013, 4:01 AM), http://kodak.boards.net/thread/5165/kodak-unipixel-partnership-valuation (analyzing publicly disclosed financial data to determine the valuation of a joint venture project); dmdmd1, *IMO...My Cram Up Plan and DCF Analysis*, KODAK BOARD (Apr. 8, 2013, 6:10 AM), http://kodak.boards.net/thread/4544/imo-cram-plan-dcf-analysis (considering an alternative plan of reorganization for the company).

186. *See, e.g.*, Letter from Luis Diaz to U.S. Trustee re: Valuation of Kodak's Patent Portfolio, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. June 5, 2013), ECF No. 3911 (arguing that the debtor's financial disclosures hugely underrated the value of the property); Letter from Sheila R. Paganini to U.S. Trustee re: Valuation of Kodak's Patent Portfolio, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. June 5, 2013), ECF No. 3908 (stating that the debtor understated the value of Kodak's patents).

187. *See* Letter from William S. Crumley to Judge Gropper re: Patents/Revenue Filed, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. July 8, 2013), ECF No. 4248 (demanding that the debtors disclose the anticipated value of royalty stream licenses and licenses of patent assets); Letter from William S. Crumley to Judge Gropper re: Sale of DC/KISS Patent Portfolio, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. July 1, 2013), ECF No. 4198 (demanding disclosure of information regarding royalty stream licenses possibly retained by the debtor after sale of assets).

188. *See, e.g.*, Letter from Matthew Glassman to Judge Gropper re: S'holder Representation, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. May 8, 2013), ECF No. 3677 (sharing data showing Kodak's potential future benefits from their multibillion dollar net operating losses).

189. *In re* Eastman Kodak Co., No. 12-10202, 2013 WL 4413300, at *1–2 (Bankr. S.D.N.Y. Aug. 15, 2013).

190. *See supra* note 102 and accompanying text (giving an example of shareholders' attempts to obtain an official equity committee and the debtor's objection thereto).

191. Daubert v. Merrell Dow Pharm. Inc., 509 U.S. 579 (1993).

all of the expert testimony.[192] At the hearing to consider the shareholders' motion, shareholders faced overwhelming opposition. In the words of one shareholder: "there were 19 lawyers sitting opposite us three stockholders and our attorney."[193]

In its opinion declining, once and for all, to appoint an official equity committee and granting the debtor's motions to exclude the shareholders' evidence, the court showed some frustration towards shareholders engaged in direct action and grassroots organization.[194] Instead of acknowledging that they had overcome considerable obstacles and recognizing that they were not receiving reimbursement of costs from the estate, the court roundly criticized them for not putting forth a more thorough valuation case.[195] The court was unreceptive to the shareholders' experts, referring to them as "witnesses purported to be experts" and repeatedly comparing them to the debtor's more prominent professional advisors who *were* securely reimbursed from the bankruptcy estate.[196] Indeed, the court ultimately excluded all of the shareholders' expert witness testimony as wholly unreliable.[197] Finally, the court subjected the shareholders' arguments to extreme reductionism, essentially characterizing them as disgruntled conspiracy theorists: "Other than the unsupported hypothesis that Kodak, Kodak's professional advisors, the Creditors' Committee, and the Committee's professional advisors are all not to be trusted, the Shareholders provided no reason whatsoever for disregarding Kodak's publicly filed financial statements and projections."[198] And with that, the shareholders' quest for a seat at the bankruptcy negotiation table ended.

192. *See, e.g.*, Notice of Motion and Debtors' Motion in Limine to Exclude all Opinion Testimony of Elise Neils at the Hearing on the S'holders' Motion for an Order Approving the Appointment of an Official Equity Comm., *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. Aug. 2, 2013), ECF No. 4546.

193. Interview with Nancy Bo (Dec. 28, 2013) (on file with the author).

194. The court made numerous references to the fact that the shareholders were unrepresented by counsel. For instance, the court noted that "different shareholders . . . acting pro se, began to file letters with the Court complaining that they would receive nothing in Kodak's reorganization case . . . . None of the letters was submitted through a lawyer." *In re* Eastman Kodak Co., No. 12-10202, 2013 WL 4413300, at *1 (Bankr. S.D.N.Y. Aug. 15, 2013). Later, the court referred to a pro se filing, as a "letter purport[ing] to be a motion." *Id.* at *2.

195. *Id.* at *4–6.

196. *Id.* at *2, *4–6. The court introduced the shareholders' experts solely by their names, excluding their professional titles and affiliations. *Id.* at *2. ("Maulin V. Shah and Elise Neils"). In contrast, the court referred to the debtor's advisors by their names, titles and professional affiliations. *In re* Eastman Kodak Co., No. 12-10202, 2013 WL 4413300, at *2 (Bankr. S.D.N.Y. Aug. 15, 2013) ("David S. Kurtz, Vice Chairman and Global Head of the Restructuring Group at Lazard Freres & Co., LLC"). Towards the end of the opinion, the court drew a starker contrast, comparing the work of Elise Neils to that of "recognized professionals." *Id.* at *6. The court discounted both the experience and professional opinions of Maulin V. Shah, Founder and Managing Director of Envision IP, referring to him as "a law graduate who had practiced for a year" before founding an intellectual property valuation firm, and referring to his uncontested points as "appear[ing] to be rooted in reality," and his contested points as "fallacious logic." *Id.* at *4–5. In the case of Elise Neils, Managing Director of Brand Finance, the court pointed out that "she or her colleagues spent a grand total of six hours before producing for the Shareholders a 'Kodak® Preliminary Brand Valuation' at 3:00 a.m. on July 26, 2013." *Id.* at *5. Finally, the court blasted the latter expert's testimony: "Even if Ms. Neils had had the opportunity in her six hours of work to learn the basic facts regarding Kodak's present financial situation—and she admitted at the hearing that she did not—she did not dispute that brand value is not a separate item of value." *Id.* at *6.

197. *In re* Eastman Kodak Co., No. 12-10202, 2013 WL 4413300, at *4 (Bankr. S.D.N.Y. Aug. 15, 2013).

198. *Id.* at *5.

Where shareholders are denied the appointment of an official equity committee, the U.S. Trustee and/or the bankruptcy court essentially conclude one of two things: that shareholders simply do not have any meaningful interests in the restructuring,[199] or that their interests are adequately represented by the debtor's management and/or by the official creditors' committee.[200] Indeed, the bankruptcy court in *Eastman Kodak* provided both justifications.[201] The latter point assumes that, to the extent creditors have become residual claimants, they arguably possess the same economic preferences as equity security holders and can be expected to advance restructuring outcomes that benefit both classes.[202] But in practice, neither the debtor's management nor an official creditors' committee may be capable of providing shareholders with adequate representation. As shareholders argued in *Eastman Kodak*, the debtor's management frequently takes an adversarial stance towards shareholders in Chapter 11 cases, particularly to the extent shareholders are viewed as an obstacle to reaching a negotiated settlement with creditors.[203] Official creditors' committees are not under any affirmative obligation to represent equity security holders, even if the court believes that they are somehow inclined to do so. In *Eastman Kodak*, the debtor's attorneys from Sullivan & Cromwell LLP made this amply clear in letters delivered to individual common shareholders: "[T]he Official Committee [of Unsecured Creditors] represents prepetition unsecured creditors (not Kodak Equity Interests)."[204] Practically speaking, the creditors' committee has no real incentive to push for a higher valuation of the debtor, such that equity holders might receive a distribution; this is especially true where the Chapter 11 plan contemplates that creditors will advance to an equity position in the reorganized company.[205]

More broadly, most official committees are comprised of the largest interest holders,[206] who may not be responsive to the needs of widely dispersed, non-insider[207]

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199. This point is cogently made in *In re* Ampex Corp., No. 08-11094, 2008 WL 2051128, at *2 (Bankr. S.D.N.Y. May 14, 2008) ("Given that none of the creditors senior to equity are receiving payment in full on behalf of their claims, there simply is no value for equity holders and thus they have no meaningful interest in the outcome of the case.").

200. Such is the conclusion of the *Williams* court: "the Creditors' Committee has sufficiently aligned or parallel interests with the Shareholders to preclude the need for an additional committee." *In re* Williams Commc'ns Grp., Inc., 281 B.R. 216, 222–23 (Bankr. S.D.N.Y. 2002).

201. *Kodak*, 2013 WL 4413300, at *2-3.

202. *Williams*, 281 B.R. at 222–23.

203. *See* Kodak S'holders' Joint Motion for Order, *supra* note 84 (asking the court to appoint an official committee of equity security holders); Letter to Judge, *supra* note 84 (asking the court to appoint an official committee of equity security holders).

204. *See, e.g.*, Letter from Andrew G. Dietderich, Partner, Sullivan & Cromwell LLP, to Joseph Dallal, Kodak Shareholder (Jul. 12, 2013) (on file with author).

205. *See In re* Pilgrim's Pride Corp., 407 B.R. 211, 218–19 (Bankr. N.D. Tex. 2009) (acknowledging conflicts of this sort).

206. *See* 11 U.S.C. § 1102 (2012) (requiring that the U.S. trustee ordinarily appoint the persons holding the seven largest claims against the debtor to the creditors' committee).

207. Insiders have other strategic advantages that enable them to negotiate for better treatment in Chapter 11. Consider the following example documented in a 1990 empirical study: "In the Dreco Energy case, insiders, who constituted management at filing, controlled 75% of the shares. They were able to secure a very favorable distribution to equity in part because their continued participation in the company was considered critical to its success." LoPucki & Whitford, *supra* note 79, at 143. The phenomenon is further explored in Jerome R. Kerkman, *The Debtor in Full Control: A Case for Adoption of the Trustee System*, 70 MARQ. L. REV. 159, 165–83 (1987);

individual investors with relatively small interests. Finally, prominent institutional investors at times engage in committee capture, steering the agenda towards promotion of their own, often conflicted, interests.[208] Indeed, even official *equity* committees are susceptible to the same problems. In light of these realities, the following Subpart considers whether the debtor's common shareholders might rely upon ad hoc groups[209]—or even dominant shareholders who participate directly in the case—to advance their interests.

C. Ad Hoc Groups; Direct Action by Large Shareholders

As the previous Subparts argue, other traditional legal structures largely fail to promote the interests of a bankrupt company's widely dispersed common shareholders. Without a seat at the negotiation table, equity owners are highly unlikely to successfully advance arguments or bargain to receive a distribution; in essence, they are preemptively crammed down. Sidestepping concerns of this sort, the *Williams* court noted that "in most cases, even those equity holders who do expect a distribution in the case can adequately represent their interest without an official committee."[210] To be fair, all equity security holders of the debtor are "parties in interest" under Chapter 11, and thus have the right to appear and be heard on issues pertaining to the restructuring;[211] in this way, they are not actually preemptively crammed down. But as the legislative history of Chapter 11 reveals,[212] and as I have argued elsewhere,[213] modern commercial bankruptcy process privileges organizational actors, such as official committees, who have a seat at the negotiation table. Because Chapter 11 relies upon party consensus and market mechanisms to reach restructuring outcomes, parties cannot simply trust the judicial process to protect their interests.[214] Without a ready seat at the negotiation table, meaningful participation effectively requires financial backing, as only official committees are assured reimbursement of costs and expenses from the debtor's estate.[215] For these reasons, the ability to organize through official committees confers a distinct structural privilege, affording certain parties the right to participate meaningfully in plan negotiations.

Lynn M. LoPucki, *The Debtor in Full Control: Systems Failure Under Chapter 11 of the Bankruptcy Code?*, 57 AM. BANKR. L.J. 99, 247, 272–73 (1983).

208. *See generally* Michelle M. Harner & Jamie Marincic, *Committee Capture? An Empirical Analysis of the Role of Creditors' Committees in Business Reorganizations*, 64 VAND. L. REV. 749 (2011) (empirically investigating these and related concerns).

209. *See generally* David L. Perechocky, *Should Ad Hoc Committees Have Fiduciary Duties?: Judicial Regulation of the Bankruptcy Market*, 86 AM. BANKR. L.J. 527 (2012) (giving scholarly attention to ad hoc groups, and proposing a number of theories that could justify imposing fiduciary duties on ad hoc groups, but concluding that nonetheless courts should not impose such duties for practical and normative reasons).

210. *In re* Williams Commc'ns Grp., Inc., 281 B.R. 216, 223 (Bankr. S.D.N.Y. 2002).

211. *See supra* note 4 (defining a "party in interest" in a Chapter 11 proceeding).

212. *Supra* note 78 and accompanying text.

213. *See generally* Dick, *supra* note 14 (challenging the idea that the use of market mechanisms will make bankruptcy proceedings more efficient).

214. *Id.*

215. 11 U.S.C. § 503(b).

Nonetheless, persons holding equity positions may come together and form ad hoc committees in Chapter 11 cases.[216] These groups at times muscle their way to the negotiation table. Historically, these informal groupings were comprised of large, institutional shareholders with the financial means to intervene in bankruptcy proceedings.[217] For instance, an ad hoc group mainly consisting of hedge funds intervened in the bankruptcy reorganization of Spansion, Inc., to object to the debtors' Chapter 11 plan and disclosure statements.[218] Recognizing the historical tendency for ad hoc committees to consist of persons with market power in the securities and capital markets, the U.S. Bankruptcy Court for the Southern District of New York noted that such committees "implicitly ask the court and other parties to give their positions a degree of credibility appropriate to a unified group with large holdings."[219]

In recent years, however, individual common shareholders with much smaller holdings have attempted to participate in bankruptcy cases through informal groupings of this sort. For instance, in the 2009 bankruptcy reorganization of Source Interlink Co., Inc., a group of individual common shareholders formed an ad hoc committee and retained counsel to pursue the appointment of an official equity committee.[220] In the Chapter 11 bankruptcy of Washington Mutual, Inc.,[221] a group of individual common shareholders formed a limited liability company to receive donations to cover the group's costs and expenses and to attempt to intervene in the proceedings.[222] Most recently, a group of Eastman Kodak Company's individual common shareholders formed an ad hoc committee and retained counsel in their final push to obtain an official equity committee and, when such requests failed, to object to the debtor's proposed Chapter 11 plan.[223]

Even where the group is not comprised of persons with sizable individual or combined holdings, ad hoc committees nonetheless allow similarly situated parties to coordinate activities and share expenses in their attempts to influence the proceedings. As the U.S.

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216. *See, e.g.*, *infra* notes 218 and 219 and accompanying text (explaining the nature and role of ad hoc committees).

217. *See infra* note 219 and accompanying text (implying that ad hoc committees were traditionally comprised of large and powerful stakeholders).

218. *See In re* Spansion, Inc., 426 B.R. 114, 118 (Bankr. D. Del. 2011) (evidencing a number of filings made by the "*Ad Hoc* Committee of Equity Security Holders").

219. *In re* Northwest Airlines, 363 B.R. 701, 703 (Bankr. S.D.N.Y. 2007).

220. Letter from David N. Ravin, Robert E. Nies & Christopher A. Ward, Co-Counsel for the Ad Hoc Committee of Equity Shareholders re: Request to Appoint an Official Committee of Equity Security Holders, *In re* Source Interlink Co., Inc., et al., No. 09-11424 (Bankr. D. Del. May 8, 2009), ECF No. 113.

221. *In re* Washington Mut., Inc., No. 08-12229 (MFW) (Bankr. D. Del.). The parent company and its affiliates filed voluntary petitions for relief under Chapter 11 of the U.S. Bankruptcy Code in the U.S. Bankruptcy Court for the District of Delaware. The cases were jointly administered as Case No. 08-12229 (MFW) under the caption "*In re* Washington Mutual, Inc."

222. United International Equity Members' Objection to the Global Settlement Agreement, *In re* Washington Mutual, Inc., Case No. 08-12229 (MFW) (Bankr. D. Del. Mar. 11, 2011), ECF No. 6925; Interview with Catherine Dziok (Aug. 21, 2013) (on file with the author).

223. *See, e.g.*, Shareholders' Objection to Debtors' First Amended Joint Chapter 11 Plan of Reorganization Filed by Ahsan Zia, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. Aug. 7, 2013), ECF No. 4658; Request for Service of Papers by Wayne M. Greenwald on Behalf of Ahsan Zia as Representative of the Ad Hoc Committee of Equity Security Holders, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. Aug. 2, 2013), ECF No. 4542.

Bankruptcy Court for the District of Delaware acknowledged: "[C]ollective action . . . through the use of *ad hoc* committees or groups allows [claimants] to utilize other group members' holdings to obtain a greater degree of influence in a bankruptcy case than single [claimants] acting alone."[224] But when it comes to advancing the interests of widely dispersed common shareholders, these arrangements are a weak substitute for formal representation, such as through the appointment of an official committee. For one thing, it is much more difficult for ad hoc committees to receive reimbursement of expenses from the debtor's estate.[225] Attorneys and other professionals retained by an ad hoc committee are only paid by the debtor's estate if they can demonstrate that the committee made a substantial contribution to the bankruptcy case.[226] Courts typically apply the test strictly, making these motions difficult to sustain.[227] Also, ad hoc committees are not a panacea because, while the law is unsettled with respect to the potential fiduciary duties of informal groupings to those they purport to represent,[228] there is presently no affirmative obligation for ad hoc equity committee members to negotiate on behalf of all shareholders.[229]

Alternatively, individual common shareholders might choose to rely on other, larger shareholders with market power in the capital and securities markets who engage directly in the Chapter 11 case on their own as parties in interest.[230] For example, in Delphi Corporation's 2005 bankruptcy reorganization, a hedge fund that held a substantial stake in the debtor's equity directly intervened in the case, retaining in the process one of the world's largest commercial law firms.[231] These actions presumably had the potential to benefit all equity security holders, including persons with much smaller stakes. But although hedge funds and other large, activist investors regularly engage in direct action in bankruptcy cases,[232] their participation is not a substitute for formal representation of widely dispersed common shareholders. For one thing, these large shareholders have their own interests, which might be influenced by their broader portfolios and investment goals. Moreover, they may be incentivized to seek excess returns, the costs of which the debtor's other common shareholders would ultimately bear. For instance, large shareholders might use their leverage to negotiate for benefits other than a distribution on account of their

224. *In re* Washington Mut., Inc., 419 B.R. 271, 279 (Bankr. D. Del. 2009).

225. 11 U.S.C. § 503(b).

226. *Id.*

227. *See, e.g.*, *In re* Mirant Corp., 354 B.R. 113, 137 (Bankr. N.D. Tex. 2006) (applying the "substantial contribution" standard to a Chapter 11 proceeding). A recent case declining to award professional fees to attorneys representing an ad hoc equity committee demonstrates the difficulty of meeting the "substantial contribution" standard. *In re* Spansion Inc., 2014 WL 1928632 (Bankr. D. Del. 2014).

228. This question was recently raised in the *Northwest Airlines* and *Washington Mutual* bankruptcy cases. *See* Perechocky, *supra* note 209, at 532–33 (describing how the *Northwest Airlines* and *Washington Mutual* courts raised the possibility of fiduciary duties for ad hoc committees).

229. *See id.* (arguing that ad hoc committees do not and should not have fiduciary duties).

230. Hedge fund activism in corporate governance matters is explored in Seretakis, *supra* note 32. In a balanced and thoughtful critique, the author considers the risks and advantages of hedge fund interventions.

231. *See* Response of the U.S. Trustee to Motion of Appaloosa Mgmt. L.P., *In re* Delphi Corp. et al., Case No. 05 B 44481 (RDD) (Bankr. S.D.N.Y. Dec. 30, 2005), ECF No. 1682.

232. The nature and consequences of these activities are explored in Jongha Lim, *The Role of Activist Hedge Funds in Distressed Firms* (2010) (Working Paper, 2010) (on file with Ohio State University), *available at* http://business.uc.edu/content/dam/business/departments/finance/docs/Jongha%20Lim_JobMarketPaper_11191 0.pdf.

equity security interests, such as participation in a pre- or post-plan confirmation credit facility bearing above-market fees and interest. These dangers are particularly acute because there is no affirmative legal obligation for shareholders who engage in direct action to negotiate on behalf of all shareholders, and shareholders generally do not owe fiduciary duties to other shareholders.[233]

Perhaps in light of these realities, Eastman Kodak Company's individual common shareholders chose not to rely solely upon ad hoc committees or the direct action of other, larger shareholders. Instead, they also sought representation from those who have taken an oath of office to serve and protect the public: the U.S. Trustee, the bankruptcy judge and other court officials, and employees of the Securities and Exchange Commission (SEC). The following Subpart considers these possible avenues for protection and advancement of shareholder interests in large commercial bankruptcies.

D. The Office of the U.S. Trustee, the Bankruptcy Court and the SEC

When all else fails, individual common shareholders of bankrupt companies may look to the U.S. Trustee to protect their interests. For instance, in *Eastman Kodak*, even after the U.S. Trustee denied the first request to appoint an official equity committee, individual shareholders posting on a message board created by and for common equity holders devised a plan to "write letters to [the U.S. Trustee for the region that includes the Southern District of New York] requesting her to support [their second attempt to obtain an official equity committee]."[234] At another point in the case, shareholders encouraged each other to reach out to the U.S. Trustee to report "insider trading and fraud allegation[s]."[235] Such reliance is fitting, as the primary role of the U.S. Trustee Program is to serve as the "watchdog" over the bankruptcy process, with the specific authority to monitor Chapter 11 plans and disclosure statements.[236] The U.S. Trustee is also designated to receive

233. *See* Global Crossing Estate Representative v. Winnick, U.S. Dist. LEXIS 53785, at *66–67 (S.D.N.Y. Aug. 3, 2006) ("[A] fiduciary duty exists only in those rare cases where a shareholder 'dominate[s] and control[s] a corporation,' and thus may be held liable 'for detriment to the corporation caused by their breach of the fiduciary obligation arising from that relationship.'").

234. Subzeroooo, *Letter to US Trustee Requesting Support for EC*, KODAK BOARD (Jul. 21, 2013, 6:52 PM), http://www.kodak.boards.net/thread/6191/letter-trustee-requesting-support-ec.

235. Godzilla, *U.S. Trustee Hope Davis in Big Trouble*, KODAK BOARD (May 22, 2013, 6:25 PM), http://kodak.boards.net/thread/5592/trustee-hope-davis-big-trouble. Responding to the original post, the same commenter posted, in all capital letters: "WE ALL NEED TO EMAIL HER."

236. S. REP. 95-595 at 5966 (1978); *see also In re* South Beach Sec., Inc., 606 F.3d 366, 370 (7th Cir. 2010) (discussing the duties assigned to the Trustee under 28 U.S.C. § 586(a)(3)); 28 U.S.C. § 586(a)(3)(B) (authorizing the U.S. Trustee to monitor Chapter 11 plans and disclosure statements); Morgenstern v. Revco D.S., Inc., 898 F.2d 498, 500 (6th Cir. 1990) (referring to the U.S. Trustee as a "watchdog"). The program was initially introduced through a pilot program in 1978, and subsequently expanded in 1986. *See* DEPT. OF JUSTICE, OVERVIEW OF THE UNITED STATES TRUSTEE PROGRAM, http://www.justice.gov/ust/eo/public_affairs/factsheet/docs/fs02.htm (last visited Sept. 11, 2014) (describing the U.S. Trustee Program).

complaints of criminal violations—such as fraud—in the bankruptcy system,[237] and the agency has recently launched independent initiatives to target bankruptcy abuse.[238]

However, as the program's mission statement foreshadows, shareholders of corporate debtors once again largely fall through the cracks: "The mission of the United States Trustee Program is to promote the integrity and efficiency of the bankruptcy system for the benefit of all stakeholders—debtors, creditors, and the public."[239] The term "equity holders" is conspicuously missing from the list of intended beneficiaries. Of course, the list of stakeholders was not necessarily intended to be exclusive.[240] Moreover, common shareholders of publicly traded corporations are also members of "the public," and thus fall within the broadest of the three named categories of beneficiaries.

But in practice, shareholders of large corporate debtors have had little success in appealing to the U.S. Trustee for assistance. As noted above, the U.S. Trustee has grown less hospitable to shareholder requests for a seat at the bankruptcy negotiation table, at times filing oppositions to requests that the court order the appointment of an official equity committee. These phenomena were fully evidenced in *Eastman Kodak*.[241] Furthermore, at least one Eastman Kodak Company shareholder experienced some difficulties in contacting the designated U.S. Trustee: "The trustee never answered my letter. She gave the wrong fax number out. At one point they moved offices and my registered letter got returned and said no one [was] there at that address."[242] In general, the U.S. Trustee tends not to intervene in large corporate bankruptcies in ways that upset the expectations of dominant stakeholders.[243]

Similarly, as another last possible vestige, shareholders of bankrupt companies may plead directly with the judge to protect their interests. In *Eastman Kodak*, individual

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237. *See* REPORTING BANKRUPTCY FRAUD, http://www.canb.uscourts.gov/%5Bfield_site_menu_category-raw%5D/reporting-bankruptcy-fraud (last visited Sept. 11, 2014) (describing the process to file bankruptcy fraud complaints to the U.S. Trustee).

238. *See* Press Release, Department of Justice, Executive Office for U.S. Trustee, U.S. Trustee Program Launches Bankruptcy Civil Enforcement Initiative (Oct. 30, 2001), *available at* http://www.justice.gov/ust/eo/public_affairs/press/docs/pr20011030.htm (outlining U.S. Trustee Civil Enforcement Initiative).

239. DEPT. OF JUSTICE, STRATEGIC PLAN & MISSION, http://www.justice.gov/ust/eo/ust_org/mission.htm (last visited Sept. 11, 2014).

240. However, if we reason by analogy and apply canons of statutory interpretation to the mission statement, then the omission is potentially more troublesome. *See* Hartford Underwriters Ins. Co. v. Union Planters Bank, N.A., 530 U.S. 1, 6–7 (2000) (noting that where "a statute . . . names the parties granted [the] right to invoke its provisions, . . . such parties only may act") (internal quotation marks and citation omitted); U.S. v. Landmesser, 378 F.3d 308, 313 n.8 (3d Cir. 2004) ("The canon of expressio unius est exclusio alterius means that explicit mention of one thing in a statute implies a congressional intent to exclude similar things that were not specifically mentioned.") (internal quotation marks and citation omitted).

241. *See supra* Part II.2 (describing the U.S. Trustee's opposition to shareholder requests in *Eastman Kodak*).

242. Interview with Nancy Bo (Jan. 2, 2014) (on file with the author).

243. This may reflect the realities of a governmental agency that interacts with a relatively small and insular insolvency and restructuring community. Indeed, in a recent incident, a bankruptcy judge on the U.S. Bankruptcy Court for the Southern District of New York publicly admonished and compared a U.S. Trustee to a "first-year law student" for her actions in a trial arising out of the U.S. Trustee's accusations of conflicts of interests and unreasonable professional fees. *See* Jacqueline Palank, *Bankruptcy Watchdog Defends Role in GSC Case*, WALL ST. J. (May 13, 2013), http://blogs.wsj.com//bankruptcy/2013/05/13/bankruptcy-watchdog-defends-role-in-gsc-case/ (describing how the U.S. Trustee defended her role in the trial).

shareholders sent dozens of heartfelt letters to the judge, with many taking a relatively informal tone and some even written by hand.[244] One such letter closed with the statement: "I hope you will remember us and look out for us. It appears nobody else is."[245] Another shareholder penned the following: "again I write to you still believing that the United States has the best legal system in the world. I'm confident that the Kodak common shareholders' 'Equity Interests' are carefully being watched over from your Courtroom."[246] Yet another shareholder explained, "I do not understand the laws. I understand that I can ask that you help to protect any rights I may have."[247]

This strategy has the potential to be successful, as the Bankruptcy Code grants the judge broad equitable powers.[248] The bankruptcy court can alter the course of bankruptcy negotiations by, among other things, "monitoring, mediating, [and] setting deadlines."[249] But the court gave Eastman Kodak Company shareholders little relief. For instance, when asked whether the court or any officers of the court attempted to represent the needs of individual common shareholders during the bankruptcy, one shareholder responded: "No, with the exception of some of the people in the clerk's office who went out of their way to make sure we were heard (or at least our letters and objections put on the docket)."[250] As the shareholders learned in their attempts to obtain an official equity committee, bankruptcy judges cannot use these broad equitable powers to protect interests that the law—as influenced by economic efficiency norms—presumes to be nonexistent. On one hand, the experience in *Eastman Kodak* may simply reflect the tendency for courts to defer to the sound business judgments of the debtor.[251] But it might also reflect a deeper "pro-debtor" behavioral bias across the bankruptcy bench.[252] This preference, to the extent it

244. *See, e.g.*, Letter from Kenneth Heinlein to Judge Allan L. Gropper, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. Jul. 1, 2013), ECF No. 4233 (appealing to the judge directly in a hand-written letter for assistance).

245. *Id.*

246. Letter from Joseph Dallal to Judge Allan L. Gropper, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. Jul. 22, 2013), ECF No. 4398.

247. Letter from Mark Bolivar to Judge Allan L. Gropper, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. Jul. 10, 2013), ECF No. 4266.

248. *See generally* 11 U.S.C. § 105(a) (2013) (giving a bankruptcy judge the broad authority to issue any order, process or judgment necessary or appropriate to carry out the provisions of the Bankruptcy Code). *See also* Brenham v. Deerfield Org., Inc. (*Matter of* Norman Indus., Inc.), 1 B.R. 162, 165 (Bankr. W.D. La. 1979) (opining that the predecessor statute of § 105(a) recognized and declared the principle that courts of bankruptcy are courts of equity).

249. LoPucki & Whitford, *supra* note 53, at 716.

250. Interview with Greg Armstrong (Dec. 6, 2013) (on file with the author).

251. The business judgment rule has been applied to bankruptcy questions. *See, e.g.*, Lubrizol Enters., Inc. v. Richmond Metal Finishers, Inc., 756 F.2d 1043, 1046–47 (4th Cir. 1985) (finding that with respect to the decision whether to assign or reject an executory contract, "the bankrupt's decision upon it is to be accorded the deference mandated by the sound business judgment rule as generally applied by courts to discretionary actions or decisions of corporate directors").

252. The phenomenon is noted in Keith Sharfman, *Judicial Valuation Behavior: Some Evidence From Bankruptcy*, 32 FLA. ST. U. L. REV. 387, 390 (2005); *see also* DAVID A. SKEEL, JR., DEBT'S DOMINION: A HISTORY OF BANKRUPTCY LAW IN AMERICA 194 (2001) (acknowledging a pro-debtor bias).

exists, implicates a broader proclivity of bankruptcy judges to be viewed as facilitators of successful reorganizations.[253]

Finally, individual common shareholders at times attempt to contact officials at the SEC, the federal agency responsible for protecting public investors and regulating and enforcing compliance with the federal securities laws. The SEC is technically a statutory party to all Chapter 11 bankruptcy proceedings, and may act as a special advisor to the courts with the power to "raise and . . . appear and be heard on any issue."[254] In *Eastman Kodak*, shareholders posting on an online message board devoted an entire sub-forum to devising a strategy to obtain the assistance of the SEC.[255] A poster explained: "We need to make the SEC aware of the fraud that is being perpetrated against the shareholders," encouraging other forum participants to post any contacts they may have at the SEC and to engage in a letter writing campaign.[256] When another poster noted that he or she already met with a person affiliated with the SEC, the original poster encouraged the shareholder to "get him and his team copies of the [filings made by shareholders to] the docket," expressing hope that "they wont [sic] believe their eyes!"[257]

The SEC has, at times, intervened in Chapter 11 cases on behalf of a debtor company's public investors. Indeed, as Professor Douglas Baird explained, the SEC's advocacy in a pivotal 1930s commercial bankruptcy case had the "consequence of firmly embedding the absolute priority rule in the law of corporate reorganizations."[258] More recently, the SEC filed a 35-page memorandum in support of an ad hoc committee's motion for the appointment of an official equity committee in the 2004 Interstate Bakeries Corporation Chapter 11 case.[259] The motion outlined public company shareholders' unique vulnerabilities, reminding the court that "no other entity can be expected to protect the common interests of . . . [common, non-insider] shareholders,"[260] and arguing in favor of the earlier, more flexible "hopelessly insolvent" standard for the appointment of an official equity committee.[261] The SEC filed a similar memorandum of law in 2009 to support

253. Greg Zipes, *Securitization: Challenges in the Age of* LTV Steel Co., Inc., 2002 ANN. SURV. BANKR. L. 105, 116 (2002).

254. 11 U.S.C. § 1109(a).

255. *See Contact SEC Regarding Kodak*, KODAK-SHAREHOLDERS.COM, http://kodak.boards.net/board/12/contact-sec-regarding-kodak (last visited Sept. 21, 2014) (discussing methods to contact the SEC).

256. Admin, *Post any and all contacts for the SEC!!!*, KODAK-SHAREHOLDERS.COM (May 11, 2013, 3:02 PM), http://kodak.boards.net/thread/5358/post-any-all-contacts-sec.

257. Admin, *Post any and all contacts for the SEC!!!*, KODAK-SHAREHOLDERS.COM (May 22, 2013, 5:26 PM), http://kodak.boards.net/thread/5358/post-any-all-contacts-sec.

258. Douglas G. Baird, *Present at the Creation: The SEC and the Origins of the Absolute Priority Rule*, 18 AM. BANKR. INST. L. REV. 591, 605 (2010).

259. Memorandum of the U.S. Sec. Exch. Comm'n in Support of the Motion of Ad Hoc Committee for Appointment of Comm. of Equity Sec. Holders, *In re* Interstate Bakeries Corp., Case No. 04-45814 (JMV) (Bankr. W.D. Ms. Nov. 9, 2004), ECF No. 549.

260. *Id.* at 2. Further, the SEC reminded the court that an "official committee charged with safeguarding the interests of the class it represents is one of the critical protections for creditors and shareholders provided in the Bankruptcy Code." *Id.* at 5.

261. *Id.*

shareholders of Pilgrim's Pride Corporation.[262] And, in several recent, high-profile corporate scandals, the SEC has intervened to reconfigure the firm's governance structure during the pendency of the bankruptcy case.[263]

But the SEC never intervened in *Eastman Kodak*. This is most likely because, in modern practice, the agency does not typically take a substantive role in most bankruptcy cases; in fact, the SEC's own website notes that "[i]n most bankruptcy cases, the role of the SEC is limited."[264] As a general rule, the SEC's role is restricted to its more traditional functions: monitoring disclosures, policing fraud, and ensuring that bankruptcy process is not used to evade securities regulations.[265] Evidencing this more customary role, the SEC recently filed an opposition to a debtor company's Chapter 11 plan on the grounds that the restructuring was a sham designed to allow a private company to go public without complying with securities registration requirements.[266]

To be sure, literature has greatly disagreed on the SEC's proper role in commercial bankruptcy cases. In their influential 1990 study, Professors LoPucki and Whitford urged the SEC to intervene in Chapter 11 cases to promote the interests of public equity investors.[267] More recently, the debate took center stage at the American Bankruptcy Institute Law Review's 2010 symposium, "The SEC in Bankruptcy: Past, Present and Future."[268] Reflecting on recent SEC interventions in high profile corporate scandals, Professor David Skeel argued that although such interventions may be appropriate in

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262. Memorandum of the U.S. Sec. and Exch. Comm'n in Support of the Motion of Ad Hoc Committee for Appointment of Comm. of Equity Security Holders, *In re* Pilgrim's Pride Corp., Case No. 08-45664 (DML) (Bankr. N.D. Tex. Apr. 27, 2009), ECF No. 1590. Following the SEC's intervention in both cases, official equity committees were appointed.

263. These efforts are detailed in Alistaire Bambach & Samuel R. Maizel, *The SEC's Role in Public Company Bankruptcy Cases Where There Is a Significant Enforcement Interest*, 2005 ANN. SURV. BANKR. L. 99 (2006); David A. Skeel, *Welcome Back, SEC?*, 18 AM. BANKR. INST. L. REV. 573, 585–86 (2010).

264. *Bankruptcy*, http://www.sec.gov/answers/bankrup.htm (last visited Feb. 16, 2014). The SEC's public statement echoes the conclusion of a 1977 study, which found that the SEC's role under the draft proposed Chapter 11, "resembles that of an amicus curiae. Its function is advisory, rather than adjudicative." Michael E. Hooton, *The Role of the Securities and Exchange Commission Under Chapter X, Chapter XI and Proposed Amendments to the Bankruptcy Act*, 18 BOSTON COLL. IND. & COMM. L. REV. 427, 429 (1977). The history of the SEC's role in commercial bankruptcies is thoughtfully laid out in David A. Skeel, Jr., *The Rise and Fall of the SEC in Bankruptcy* (Univ. of Pa. Law Sch. Inst. for Law and Econ., Working Paper No. 267, 1999), *available at* http://ssrn.com/abstract=172030.

265. These are the so-called traditional functions of the SEC. Skeel, *supra* note 263, at 581–82. Yet even in respect of these traditional functions, the SEC does not place any special emphasis on bankrupt companies. A recent empirical study of securities class actions acknowledges "no statistically significant difference in the percentage of . . . parallel SEC actions for bankruptcy cases." James J. Park, *Securities Class Actions and Bankrupt Companies*, 111 MICH. L. REV. 547, 569 (2013).

266. *See* Tiffany Kary, *Edison Mission Bankruptcy Reorganization Opposed by SEC*, BLOOMBERG.COM (Feb. 11, 2014), http://www.bloomberg.com/news/2014-02-11/Edison-mission-bankruptcy-reorganization-opposed-by-sec.html (explaining the SEC's opposition to Edison Mission Energy's bankruptcy reorganization because it envisioned a scenario in which a "public shell, cleansed of liabilities, can be marketed to private companies that want to go public through a reverse merger and avoid the usual registration requirements of securities law").

267. LoPucki & Whitford, *supra* note 79, at 193 ("We believe that the SEC has played a valuable role in the cases in our study and that it should remain active in the reorganization of large, publicly held companies. The Commission's most important function has probably been as a catalyst in the formation of equity committees.").

268. G. Ray Warner & Keith Sharfman, *The SEC in Bankruptcy*, 18 AM. BANKR. INST. L. REV. 569 (2010).

egregious cases, the SEC's systematic involvement in substantive restructuring matters beyond disclosure monitoring and anti-fraud activities threatens the efficient and equitable administration of bankruptcy cases.[269] Furthering this view, Professor Kelli Alces argued that the SEC should focus its limited resources on non-bankrupt companies and remain on the sidelines in bankruptcy cases, where other systems are in place to protect investors.[270]

While the theoretical question of proper interagency balance remains unresolved, the SEC's conduct in recent years suggests that public equity investors cannot reasonably rely upon the agency to represent their interests in large commercial bankruptcies. The SEC's intervention in Chapter 11 cases remains the exception rather than the rule, particularly in those jurisdictions that regularly hear large commercial bankruptcy cases.[271] The SEC is not equipped to serve as a potential source of representation for public shareholders in Chapter 11 cases. Alistaire Bambach, Chief Bankruptcy Counsel to the Division of Enforcement of the SEC, recently explained that a "small group of dedicated bankruptcy lawyers . . . work at the [SEC]: fewer than 20, including about four appellate lawyers."[272]

In sum, the traditional legal structures simply do not provide adequate representation to the debtor's widely dispersed common equity owners. As a result, the collective action obstacles shareholders of large corporations face are significantly magnified upon the corporation's filing for bankruptcy protection. Shareholders continue to face the difficulties of organizing widely dispersed owners with divergent economic interests, no longer the exclusive beneficiary of corporate fiduciary duties. In addition, they are frequently denied the benefit of an official committee to engage in Chapter 11 plan negotiations. Indeed, the courts most likely to hear large commercial bankruptcy cases are the most hostile to requests by shareholders to appoint official equity committees. Even where official committees theoretically exist to promote equity security holders' interests, these representative bodies are vulnerable to capture by dominant interests and may not be responsive to the needs of widely dispersed common shareholders. Finally, attempts to solicit support from the U.S. Trustee, the bankruptcy court and the SEC are generally unsuccessful. Thus, notwithstanding the *Williams* court's optimistic belief that shareholders can be adequately represented even without the ready seat at the bankruptcy negotiation table that only an official equity committee can provide,[273] shareholders are systematically disenfranchised. And, without a voice in the proceeding, it is highly unlikely that they will successfully advance arguments or negotiate to receive a distribution. In essence, they are effectively subject to a preemptive cram down—albeit without the limitations and procedural protections envisioned for such a drastic mechanism.

Eastman Kodak Company shareholder Robert Saikaley eloquently captured the predicament of individual common shareholders of large, publicly traded debtor

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269. *See generally* Skeel, *supra* note 263 (discussing the SEC's governance experiments in the WorldCom and Parmalat cases).

270. Kelli A. Alces, *Limiting the SEC's Role in Bankruptcy*, 18 AM. BANKR. INST. L. REV. 631, 631 (2010).

271. *See supra* notes 264–266 and accompanying text (noting the SEC's roles in some of these jurisdictions).

272. Alistaire Bambach, *The SEC in Bankruptcy: Past and Present*, 18 AM. BANKR. INST. L. REV. 607, 607 (2010).

273. *See In re* Williams Commc'ns Grp., 281 B.R. 216, 223 (Bankr. S.D.N.Y. 2002) ("[E]ven those equity holders who do expect a distribution in the case can adequately represent their interest without an official committee and can seek compensation if they make a substantial contribution in the case.").

corporations: "Our interest has not been looked after [during the pendency of the Chapter 11 case]; not by the Trustee, not by the CEO, not by the SEC, and nor the [Board of Directors] either . . . . We have been ignored at every turn."[274] Nonetheless, many individual common shareholders refused to remain silenced and strived to resist the cram down by continuing to engage in direct action and grassroots organization for the duration of the Chapter 11 case. The following Subparts explore how and why these individual common shareholders continued to strive to gain a seat at the bankruptcy negotiation table, notwithstanding the failure of traditional legal structures to meet their needs.

III. THE ROLE OF GRASSROOTS SHAREHOLDER ACTIVISM

The story of Eastman Kodak Company shareholders' efforts to gain a voice in the bankruptcy and resist the cram down illustrates the ways in which individual common shareholders use direct action and grassroots organization to try to overcome their collective action obstacles. As noted above, common shareholders began to interact online via message boards early in the case,[275] hoping to obtain a seat at the negotiation table by persuading the U.S. Trustee and the court to appoint an official equity committee. The debtor and its creditors, and ultimately the U.S. Trustee and the U.S. Bankruptcy Court for the Southern District of New York, all claimed that equity security holders had no meaningful economic interest in the restructuring.[276] But shareholders believed that there was significant equity value in the corporation; and, at the very least, that the debtor's financial disclosures were incomplete, inaccurate or misleading because they failed to reflect the fair market value of substantial portions of the estate.[277] The shareholders' requests were twice denied, as the court relied upon *Williams* to deny the "extraordinary relief" of an official equity committee.[278]

Even now, in the wake of a confirmed Chapter 11 plan, it is difficult to know who was right and who was wrong with respect to Eastman Kodak Company's equity value. What is clear is that the court made no substantive determination, even though the debtor's valuation essentially provided the legal basis for denying shareholders a seat at the negotiation table.[279] Under the modern jurisprudence, the debtor simply enjoyed the benefit of the doubt, while shareholders shouldered a nearly impossible burden of proof.

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274. S'holders' Motion for an Order Approving the Appointment of an Official Equity Comm., *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. Jul. 23, 2013), ECF No. 4407.

275. *See, e.g.*, *Kodak Shareholders' Blog*, http://kodak.boards.net/ (last visited Jan. 24, 2014) (establishing a web forum for individual shareholders of Eastman Kodak Company during the pendency of its Chapter 11 case).

276. *See supra* notes 102–106 and sources cited therein (articulating this basic argument against the formation of an official equity committee).

277. S'holders' Motion for an Order Approving the Appointment of an Official Equity Comm., *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. Jul. 23, 2013), ECF No. 4407.

278. *In re* Eastman Kodak Co., No. 12-10202 (ALG), 2013 WL 4413300, at *2 (Bankr. S.D.N.Y. Aug. 15, 2013).

279. Recall that in its consideration of shareholders' first request for an official equity committee, the *Eastman Kodak* court declined to consider shareholders' evidence of the debtor's solvency. It noted that "[a]ny potential benefit to conducting [a valuation trial] is outweighed by the considerable time and expense it would impose on Kodak at this stage of its reorganization." *In re* Eastman Kodak Co., No. 12-10202, 2012 WL 2501071, at *3 (Bankr. S.D.N.Y. June 28, 2012). In its consideration of shareholders' second request for an official equity committee, the court heard testimony with respect to the debtor's valuation, but ultimately excluded much of the

Following the court's second denial of an official equity committee in *Eastman Kodak*, shareholders continued their attempts to participate in the case and resist the cram down, but remained wholly reliant from that point forward on their direct action and grassroots organization. Through these efforts, they worked to advance two arguments: that some of the debtor's creditors were engaged in insider trading in Eastman Kodak Company bonds and should therefore have their claims set aside,[280] and that the debtor's proposed Chapter 11 plan ought not be confirmed because it failed to meet statutory requirements.[281] Perhaps evidencing the difficulty—even for expressly enumerated parties in interest—of successfully advancing substantive arguments in Chapter 11 cases without a seat at the negotiation table, neither argument gained any traction in court. In fact, within days of denying the shareholders' second request for an official equity committee, the court confirmed the debtor's proposed Chapter 11 plan over the shareholders' objections.[282]

The fact that individual common shareholders were largely denied meaningful representation and forced to engage in grassroots activism in their final, unsuccessful push to advance their interests reminds us that there are a variety of ways in which bankruptcy law privileges economic efficiency goals at the expense of procedural fairness. It also reveals how firms and their dominant stakeholders use Chapter 11 to exploit weaker constituents who lack a ready seat at the negotiation table and who naturally have a difficult time mobilizing on their own behalf. Granted, shareholders' collective action obstacles are not limited to Chapter 11 or the bankruptcy context more broadly.[283] What is noteworthy, however, is that shareholders must overcome these enormous obstacles simply to contest the legal basis and economic justifications for disenfranchising shareholders of bankrupt companies in the first place. The frustratingly circular logic effectively sends shareholders down the proverbial rabbit hole, leaving more powerful parties free to allocate the company's economic value amongst themselves.

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shareholders' evidence. *See supra* notes 194–197 and accompanying text (describing the court's lack of appreciation for the grassroots efforts of shareholders). In its latter decision, the court ruled that the moving shareholders had not met their burden of demonstrating that they would be entitled to a meaningful distribution. *In re* Eastman Kodak Co., 2013 WL 4413300, at *7 (Bankr. S.D.N.Y. Aug. 15, 2013). It reached this decision by relying upon the debtor's own projections and asset valuations, as well as midpoints of aggregated estimated claims—the very same inputs that the shareholders sought to contest. *Id.* at *3. Thus, the court never needed to make a more precise substantive determination regarding the debtor's valuation. *Id.* at *7 (concluding that "[b]ased on the foregoing, there is no evidence that the Debtor or creditors are hiding value or that an equity committee would be appropriate, much less 'necessary' in Kodak's case").

280. *See, e.g.*, Letter from Dave M. Dayon to Judge Gropper re: Equity Committee/Bond Trading, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. May 24, 2013), ECF No. 3774 (establishing these arguments earlier in the case).

281. Objection by Greg Armstrong, S'holder (Pro Se) to the First Amended Joint Chapter 11 Plan of Reorganization of Eastman Kodak Co. and Its Debtor Affiliates, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. Aug. 12, 2013), ECF No. 4737.

282. Findings of Fact, Conclusions of Law and Order Confirming the First Amended Joint Chapter 11 Plan of Reorganization of Eastman Kodak Co. and Its Debtor Affiliates Pursuant to Chapter 11 of the Bankr. Code Chapter 11, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. Aug. 23, 2013), ECF No. 4966.

283. *See, e.g.*, Alces, *supra* note 37, at 719 ("The shareholder collective action problem is blamed for many shortcomings of corporate law.").

Relying upon the qualitative case study method, this Part develops a deeper understanding of the methods and motivations of grassroots shareholder activism in large commercial bankruptcies. Specifically, it draws upon direct observation of grassroots shareholder activism,[284] in-depth interviews with grassroots shareholder activists, and analysis of documents produced and disseminated by activists. This Article discusses the Eastman Kodak Company bankruptcy as a case study because it is a recent large commercial case in which parties, including individual common shareholders, actively litigated the potential appointment of an official equity committee. I reviewed the company's bankruptcy case docket, conducted searches and analyzed documents that individual common shareholders filed. I identified potential interview respondents through their filings made on the case docket and by postings on message boards operated by shareholders.[285] I engaged in multiple readings of documents, correspondence and web postings in an effort to identify common themes.[286] In particular, my analysis focused on the factors that influenced the shareholders' decisions to engage in direct action and grassroots organization, the methods they utilized, and the difficulties they encountered in the course of the bankruptcy case. As the following Subparts reveal, themes such as unjust corporate enrichment and abuse of legal process by dominant stakeholders emerged. These findings invite a reexamination of ownership and control in the modern corporation, as well as a reconsideration of the ways in which corporate and bankruptcy laws privilege dominant stakeholders in times of corporate financial distress.

A. Motivations for Grassroots Shareholder Activism

The following Subparts outline several broad themes regarding the motivations for grassroots organization and direct action by the Eastman Kodak Company shareholders I encountered. First, these shareholders did not merely view themselves as detached and passive investors, but rather as true owners of the company. Second, while most of them sensed that Chapter 11 case outcomes reflect the relative market power of corporate stakeholders, they nonetheless felt a strong desire to participate in the restructuring because of their longstanding relationship with the company. In other words, while the shareholders I encountered seemed acutely aware of the difficulties they faced in attempting to influence the proceedings, they felt motivated to make a last ditch effort of sorts to defend their ownership interest.

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284. This Article relies upon a relatively small number of observations, mostly arising from the same case study. This so-called small-N problem has been explored in social science literature on qualitative methodology. *See generally* James Mahoney, *Qualitative Methodology and Comparative Politics*, 40 COMP. POL. STUD. 122 (2007) (discussing the new emphasis on publications using qualitative methodology and small-N methods in the field of comparative politics).

285. Specifically, I contacted prospective interview respondents via the e-mail addresses included on their court filings, and/or through the private messaging systems on online message boards.

286. Identifying common themes across qualitative data sources—such as field notes, interview transcripts, or documents—is a recognized qualitative research method. *See, e.g.*, MATTHEW B. MILES ET AL., QUALITATIVE DATA ANALYSIS: A METHODS SOURCEBOOK 277–80 (3d ed. 2014) (discussing strategies for identifying themes by drawing from a variety of qualitative data sources).

1. Shareholder Perceptions Regarding the Meaning of Equity Ownership in the Modern Corporation

The individual common shareholders encountered in this project seemed to understand that equity investments are inherently risky. However, they perceived themselves to be owners of the bankrupt company and held firmly to this role. Although they seemed to implicitly recognize that ownership and control are separated in the modern corporation,[287] such that shareholders cannot make decisions on behalf of the company, they expected to have their interests taken into consideration throughout its lifespan. For example, an individual common shareholder of Eastman Kodak Company reminded the court: "Until this bankruptcy is settled, we the Kodak shareholders OWN this company. As owners, it is only just to allow our voices to be heard in its path to reorganization."[288] While no shareholder articulated an expectation to receive any sort of guaranteed return on his or her investment in Eastman Kodak Company, all of the shareholders encountered in this study expressed a demand for adequate representation. The shareholders believed that they were either steered by faithless fiduciaries[289] or that they were entirely left without representation.[290] As the following Subpart explores, these shareholders sensed that parties with more affluence had an easier time gaining influence in the case.

2. Shareholder Perceptions Regarding the Relationship Between Market Power and Influence

The shareholders encountered seemed to be acutely aware that unequal market power in the capital and securities markets impacts relative influence in Chapter 11 proceedings. Indeed, this is not a new phenomenon, and bankruptcy courts are not the only setting wherein affluence seems to positively correlate with influence.[291] Nonetheless, most shareholders mentioned at least one economic power dynamic that had the potential to impact the proceedings, and many expressed frustration that the commercial restructuring process under Chapter 11 seemed to reward powerful actors. For instance, in a lively objection, one shareholder remarked:

> It is truly fascinating to watch the large players in our financial markets, the management of our largest publicly-traded companies, highly-paid attorney and professional advisors, our courts, and our government oversight offices in action. But it really isn't funny, either to me or to the countless other individuals whose

287. *See supra* note 36 and sources cited therein (highlighting that stockholders do not have "legal control" over corporations, even if they enjoy distributed ownership).

288. Letter from Anthony Pillari to Judge Allan L. Gropper, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. Jul. 22, 2013), ECF No. 4406.

289. *See, e.g.*, *supra* note 68 and source cited therein (showing the shareholders' request for an Official Equity Committee to "protect the interest of common shareholders." Ahsan Zia, on behalf of the other non-insider common shareholders, discusses that little to no communication has been had between them and the ad hoc committee, and the shareholders feared they were being deliberately steered in a way that would inevitably impair their interests.).

290. *Supra* note 274 and accompanying text.

291. For a fascinating, award-winning study of the phenomenon, see GILENS, *supra* note 22 (showing and explaining the patterns of political representation seen in America over the past several decades and how the public's policy preferences relate to the actual policies that political representatives adopt in Washington).

> lives are being direly [sic] and detrimentally affected by what transpires in these cases.[292]

Frustrated by the perceived injustice of a Chapter 11 plan that contemplated cancelling the debtor's existing equity interests, the shareholder wished that the company's management would stand up for shareholders and "[t]ell the hyenas from Wall Street to go chew on some other carcass."[293] Similarly, reacting to the obvious power differentials within the case, another shareholder succinctly summarized his investment-backed expectations for a level playing field: "I am a single common shareholder that believes in the notion that the equity markets, which Eastman Kodak and many other iconic companies are traded in, are fair and transparent."[294] At the same time, he warned that if justice did not ultimately prevail in the case, it would send a powerfully negative signal to public investors everywhere:

> If Wall Street, the governing regulators, and the US [sic] Court System want to promote confidence and transparency among the markets, whether it's in the equity, bond, or debt markets, retail common shareholders need to be reassured that they are not being exploited, otherwise the whole process and idea of having open markets will never succeed.[295]

Although the shareholders encountered seemed to recognize that they faced a substantial uphill battle to gain influence in the case, many communicated their belief that a primary role of the bankruptcy court—as a court of law responsible for the administration of the case—was to protect the public investors' interests. One Eastman Kodak Company shareholder explained: "We need our voices heard your Honour to protect the interests of common shareholders [and] we need justice to prevail in your courtroom."[296] Indeed, many of the filings made by individual common shareholders included an explicit prayer for "justice."[297]

On one hand, some Eastman Kodak Company shareholders felt compelled to implicitly or explicitly acknowledge that they were *not* part of the powerful, economic elite, perhaps in the hopes that the court might be sympathetic to their interests and more inclined to take a protective stance. To this end, some shareholders mentioned their familial and socioeconomic circumstances. One shareholder referred to himself as a "family man

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292. Objection by Greg Armstrong, S'holder (Pro Se) to the First Amended Joint Chapter 11 Plan of Reorganization of Eastman Kodak Co. and Its Debtor Affiliates, at 1, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. Aug. 12, 2013), ECF No. 4737.

293. *Id.* at 50.

294. Letter from Dave M. Dayon to Judge Allan L. Gropper, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. May 24, 2013), ECF No. 3774.

295. *Id.*

296. S'holders' Motion for an Order Approving the Appointment of an Official Equity Comm. at 2, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. July 22, 2013), ECF No. 4407.

297. *See, e.g.*, Objection by Greg Armstrong, S'holder (Pro Se) to the First Amended Joint Chapter 11 Plan of Reorganization of Eastman Kodak Co. and its Debtor Affiliates, at 3, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. Aug. 12, 2013), ECF No. 4737 ("I firmly believe that 'justice' is the ultimate aim of our laws."); S'holders' Motion for an Order Approving the Appointment of an Official Equity Comm., at 2, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. July 9, 2013), ECF No. 4249 ("What kind of justice is this? Your honor, we need you to serve real justice and protect the interest of common shareholders.").

with two very young children."[298] Another explained: "Your honor, I may be from a poor family of 8 children from Rochester, New York but my parents did not raise a dummy."[299] The shareholder went on to request:

> In the name of truth, justice and the AMERICAN WAY . . . [sic] I ask for an Equity Committee to be appointed as soon as possible so that the citizens of the world can see that the United States protects the rights of the individuals . . . [sic] even against a bevy of armies . . . all armed with high paid attorneys.[300]

On the other hand, shareholders at times attempted to establish and invoke their own individual or combined economic power by referencing their relatively large share holdings. One shareholder made reference to his "16,250 shares of common stock" in Eastman Kodak Company;[301] another mentioned the "many other shareholders who hold many millions of shares."[302] Yet another shareholder referenced her large number of equity shares held in multiple accounts.[303]

Finally, some shareholders attempted to appeal to the judge's sympathies by articulating their emotional reactions to the Chapter 11 proceedings. One shareholder noted: "Your Honour, Kodak common shareholders have been suffering financially and emotionally for many years with the most suffering brought on by the debtor's bankruptcy filing."[304] Another shareholder addressed the bankruptcy judge thusly: "You are a kind and compassionate man and we appreciate the time you have spent reading our letters and listening to our pain."[305] Yet another shareholder explained, "I have worked very hard all my life as a nursing supervisor and now as a private duty nurse. I am 63 years old and my retirement money is 95% in KODAK."[306] However, the strongest emotional responses tended to focus upon shareholders' unwavering dedication to, and passion for, the bankrupt company, either because of their longstanding history as an investor or, in some cases, as an employee of Eastman Kodak Company. The following Subpart considers these motivations in greater detail.

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298. Letter from Joseph Dallal to Judge Allan L. Gropper, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. July 22, 2013), ECF No. 4398.

299. Letter from Nancy Bo to Judge Allan Gropper, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. July 22, 2013), ECF No. 4409.

300. *Id.*

301. Letter from Mark Bolivar to Judge Allan L. Gropper, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. July 10, 2013), ECF No. 4266.

302. Letter from Anthony Pillari to Judge Allan L. Gropper, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. July 22, 2013), ECF No. 4406.

303. E-mail from Nancy Bo to Judge Allan L. Gropper and the U.S. Trustee, (May 21, 2013) (on file with the author).

304. S'holders' Motion for an Order Approving the Appointment of an Official Equity Comm., at 3, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. July 9, 2013), ECF No. 4249.

305. Letter from Matt Glassman to Judge Gropper re: Unsecured Creditors/S'holders at 1, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG), (Bankr. S.D.N.Y. Aug. 9, 2013), ECF No. 4714.

306. E-mail from Nancy Bo to Judge Allan L. Gropper and the U.S. Trustee (May 21, 2013) (on file with the author).

3. Shareholders' Loyalty to the Debtor Corporation

Another theme that emerged from my research is that deep and longstanding loyalty to Eastman Kodak Company seemed to motivate individual common shareholders to attempt to influence the bankruptcy proceedings. Many of the shareholders I encountered expressed a belief that the company's common equity owners had been more loyal to the company than any other stakeholders, including its officers and directors. For instance, a shareholder closed one of his letters to the court with the declaration: "Kodak's future is bright and us loyal shareholders deserve to be a part of it."[307] Another shareholder pleaded with the court to "protect our interest, to protect the future of thousands of American families, to protect those who bought Kodak, and want to move with Kodak in the future."[308] Yet another explained: "I am a construction inspector, and I understand how difficult and sometimes pointless it is to go against the grain. I fight the fight. I also worked at Kodak as a younger man."[309] In the same letter, the shareholder referenced Eastman Kodak Company as "our company," and reminded the court of the company's motto.[310] Another shareholder implicated the passion and charisma of the company's founder, George Eastman, quoting his biography in an e-mail to the judge and concluding: "I feel with all my heart, mind and soul that George Eastman would be standing up for his shareholders."[311]

Perhaps it was this unyielding loyalty and dedication that emboldened so many of the company's individual common shareholders to engage in the process of mobilization. They were driven to take on this challenge notwithstanding the pronounced obstacles they faced under modern corporate and bankruptcy laws. The following Subpart considers the methods used by individual common shareholders in their attempts to gain a meaningful voice in *Eastman Kodak.*

B. Methods of Grassroots Shareholder Activism

Once individual common shareholders decide to participate in Chapter 11 bankruptcy proceedings, they face a number of practical limitations in addition to the collective action and legal obstacles set forth in previous sections. For one thing, individual common shareholders are frequently unable to depend upon attorneys, accountants, and other professionals to develop and refine their arguments. This is because, without the appointment of an official equity committee, shareholders are unlikely to receive reimbursement of costs and expenses from the bankruptcy estate.[312] Moreover, because large, publicly traded debtors and their creditors typically engage the most prominent

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307. Letter from Kenneth Heinlein to Judge Allan J. Gropper, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. July 8, 2013), ECF No. 4233.

308. S'holders' Motion for an Order Approving the Appointment of an Official Equity Comm., at 3, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. July 9, 2013), ECF No. 4249.

309. Letter from Mark Bolivar to Judge Allan L. Gropper, at 1, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. July 10, 2013), ECF No. 4266.

310. *Id.*

311. E-mail from Nancy Bo to Judge Allan L. Gropper and the U.S. Trustee (May 21, 2013) (on file with the author).

312. *See supra* notes 225–227 and accompanying text (explaining why ad hoc committees and individual interest holders have difficulties receiving reimbursements from bankruptcy estates).

professionals in a relatively small commercial restructuring service industry, shareholders may have a difficult time finding professionals who possess the experience and industry recognition needed to impress the court. Indeed, these challenges were fully evident in *Eastman Kodak*.[313]

Thus, individual common shareholders tend to do their own research using primary and secondary sources, materials produced by other parties, and data collected via the Internet.[314] At times, they also contact other persons involved in the case for assistance. For example, an Eastman Kodak Company shareholder explained that he "followed the case through . . . KCC, [an online claims agent website that includes the case docket], [and] had one phone conversation with the US [sic] Trustee's office."[315] Some even reached out to shareholders who attempted to intervene in other large corporate bankruptcies in an effort to learn from their experiences. For example, a poster on an online message board for Eastman Kodak Company shareholders noted that he "just got off the phone with [a] shareholder who was involved with several chapter 11 cases in the past, and is a holder of Kodak."[316]

The shareholders I encountered tended to use data and information in natural and spontaneous ways to support their claims and assertions. For instance, one shareholder cited an earlier opinion of the U.S. Bankruptcy Court for the Southern District of New York in the hopes that it would bolster her arguments.[317] Meanwhile, a different shareholder chose to append secondary articles, written by practicing attorneys, summarizing the grounds for appointment of official equity committees.[318] Another excerpted news articles in his letter to document potential insider trading by certain creditors in the case.[319] Yet another shareholder filed a multi-part analysis challenging the debtor's valuation of the company by drawing upon the debtor's own admissions reflected elsewhere on the docket, in publicly available data,[320] and in secondary sources.[321]

313. *See supra* note 196 and accompanying text (evidencing the stark contrast drawn by the court between the debtor's experts and those hired by shareholders).

314. For instance, individual common shareholders participating in an online message board conducted Internet searches to determine comparable real property valuations in Rochester, New York, and compared such data to the debtor's own valuation data. *See* it2012, *Price per acre in Rochester = 2–5 million per acre*, KODAK-SHAREHOLDERS.COM (June 24, 2013, 9:51 AM), http://kodak.boards.net/thread/5973/price-acre-rochester-2-5 (pondering property values in Rochester).

315. Interview with Greg Armstrong (Dec. 6, 2013) (on file with the author).

316. Admin, *Insider Trading Letter Docket 3774 Has Hit!*, KODAK-SHAREHOLDERS.COM (May 24, 2013, 8:00 AM), http://kodak.boards.net/thread/5595/insider-trading-letter-docket-3774.

317. Letter from Nancy Bo to Judge Allan Gropper, at 1–2, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. Jul. 22, 2013), ECF No. 4409.

318. S'holders' Motion for an Order Approving the Appointment of an Official Equity Comm., at 22–25, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. Jul. 9, 2013), ECF No. 4249.

319. Letter from Dave M. Dayon to Judge Gropper re: Equity Committee/Bond Trading, at 1–2, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. May 24, 2013), ECF No. 3774 (excerpting a Business Wire article reporting on an Eastman Kodak Company bond offering).

320. The previously referenced shareholder also utilized publicly available data, drawing data points from the debtor's previous SEC disclosures to bolster his arguments. *Id.* (citing to the debtor's SEC filings).

321. *See, e.g.*, Props. Worldwide, Plants Worldwide, Blds. Worldwide & Equip. Worldwide Filed by Robert Saikaley, at 2, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. June 20, 2013), ECF No. 4234 (listing some of the debtors' properties and raising questions about their assessment).

As noted above, the shareholders I encountered seemed to rely largely upon the Internet to come together and brainstorm possible arguments and strategies. At times, shareholders crowdsourced[322] their analyses, contributing their own expertise or enlisting volunteer assistance from friends, relatives, and other shareholders. For instance, Eastman Kodak Company shareholder and Scribd.com user "stockboardguy" provided form letters and filings through an online digital library, which other shareholders could then modify as needed, print, sign, and add to the case docket.[323] Similarly, a poster on an online message board prepared a form letter to the U.S. Trustee to encourage other Eastman Kodak Company shareholders to sign and send under their own names.[324]

However, while individual common shareholders face tremendous practical limitations in their efforts to synthesize data and develop responses, many are nonetheless able to conduct highly sophisticated analyses on their own behalf. Many Eastman Kodak Company shareholders demonstrated extensive familiarity with the case docket using the defined terms established across hundreds of complex documents prepared on behalf of the debtor by leading commercial law firms. For example, a form letter drafted by an individual shareholder concisely summarized key aspects of the debtor's proposed Chapter 11 plan including an exhibit cross-referencing dozens of docketed items.[325] Similarly, shareholder James Hurst filed his own alternative Chapter 11 plan, addressing the highly nuanced federal income tax consequences of the debtor's proposed plan.[326] And shareholder Greg Armstrong filed a thorough and well-written objection to the debtor's proposed plan, which raised a number of important questions with respect to the debtor's valuation of its assets, the transfer of non-debtor property as part of the reorganization, and related concerns.[327]

Nonetheless, as explained in previous sections, individual common shareholders were unsuccessful in their attempts to influence the proceedings in *Eastman Kodak*. Without a seat at the negotiation table, their "party in interest" status under the Bankruptcy Code meant very little: they simply did not have a meaningful platform from which they could effectively raise substantive arguments. In essence, the denial of an official equity committee had the practical effect of preemptively cramming them down. Accordingly, the

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322. The term "crowdsourcing" refers to the practice of solving problems or achieving project goals by soliciting contributions from large and diverse pools of individuals working remotely and collaborating via the Internet. *See* Jeff Howe, *The Rise of Crowdsourcing*, WIRED, June 2006, at 176, *available at* http://www.wired.com/wired/archive/14.06/crowds.html (explaining the practice and relating successful "crowdsourcing" stories); *see also, e.g.*, Jerry Brito, *Hack, Mash, & Peer: Crowdsourcing Government Transparency*, 9 COLUM. SCI. & TECH. L. REV. 119 (2008) (providing an overview of "crowdsourcing" and detailing the methods generally used by individuals crowdsourcing a solution to a problem).

323. STOCKBOARDGUY'S PROFILE, http://www.scribd.com/stockboardguy/documents (last visited Sept. 11, 2014).

324. CSwift71, *Insider Trading Letter Docket 3774 Has Hit!*, KODAK-SHAREHOLDERS.COM (May 22, 2013, 12:08 PM), http://kodak.boards.net/thread/5595/insider-trading-letter-docket-3774.

325. Stockboardguy, *Objection Letter-13*, SCRIBD.COM (Aug. 14, 2013), http://www.scribd.com/doc/160072394/Objection-Letter-13.

326. Objection by James E. Hurst to the First Amended Plan of Reorganization and Proposed First Alternative Plan of Reorganization, at 1, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. Jul. 8, 2013), ECF No. 4247.

327. Objection by Greg Armstrong, S'holder (Pro Se) to the First Amended Joint Chapter 11 Plan of Reorganization of Eastman Kodak Co. and Its Debtor Affiliates, at 4–24, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. Aug. 12, 2013), ECF No. 4737.

court approved the debtor's proposed Chapter 11 plan without modifications to address the substantive issues raised in the shareholders' many letters, motions, and objections. It seems that modern corporate and bankruptcy law—particularly in the wake of *Williams*—has erected a virtually insurmountable barrier to entry for individual common shareholders in most cases. And so, the victory of economic efficiency arguments in Chapter 11 comes at the expense of shareholders' procedural and substantive rights. The following Subpart provides a postscript of sorts, which considers the reactions of individual common shareholders to the Eastman Kodak Company restructuring.

C. A Postscript to Eastman Kodak*: Shareholder Responses to the Restructuring Outcome*

Over the many objections of common shareholders, the U.S. Bankruptcy Court for the Southern District of New York approved Eastman Kodak Company's proposed Chapter 11 plan in August 2013.[328] The shareholders I encountered in this project, like all of the company's historical equity owners, were wiped out in the restructuring.[329] Meanwhile, the reorganized Eastman Kodak Company commenced trading on the New York Stock Exchange under the ticker "KODK," reaching a 52-week high of $37.73 per share in early 2014.

Although we might expect shareholders to regret losing their financial investment, the reactions of some shareholders to the Eastman Kodak Company restructuring primarily centered upon their feelings of frustration with a process that they perceive to be extremely unfair. When asked how well the process met the needs of individual common shareholders during the bankruptcy, one shareholder responded that the process treated the shareholders "[w]ith complete and total disdain."[330] He further stated that "the process was not fair, at all."[331] In the wake of this experience, he has lost his faith in the U.S. financial markets: "Wall Street won't be getting any more of my money."[332] More recently, he explained: "The Kodak bankruptcy shook (and in fact shattered) the very foundation of my belief [in the] system as it concerns our nation's principles, its laws, and the application of those laws."[333] A poster on an online message board for Eastman Kodak Company shareholders remarked in response to the query "Has anyone learned anything from this experience that we can apply to the next investment opportunity?" the following: "the market is corrupt and manipulated . . . but pretty much knew that already. This was just another reminder."[334]

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328. Findings of Fact, Conclusions of Law and Order Confirming the First Amended Joint Chapter 11 Plan of Reorganization of Eastman Kodak Co. and Its Debtor Affiliates Pursuant to Chapter 11 of the Bankruptcy Code Chapter 11, at 64, *In re* Eastman Kodak Co., Case No. 12-10202 (ALG) (Bankr. S.D.N.Y. Aug. 23, 2013), ECF No. 4966 [hereinafter Findings of Fact, Conclusions of Law and Order]; *see also, e.g.*, Nick Brown, *U.S. Judge Approves Kodak Plan to Exit Bankruptcy*, REUTERS (Aug. 20, 2013), http://www.reuters.com/article/2013/08/20/us-kodak-idUSBRE97J0W820130820?feedType=RSS&feedName=businessNews (reporting that U.S. Bankruptcy Judge Allan Gropper approved Kodak's bankruptcy plan).

329. Findings of Fact, Conclusions of Law and Order, *supra* note 328, at 35–36.

330. Interview with Greg Armstrong (Dec. 6, 2013) (on file with author).

331. *Id.*

332. *Id.*

333. Interview with Greg Armstrong (Feb. 20, 2014) (on file with author).

334. CSwift71, *Reply to Has Anyone Learned Anything?*, KODAK-SHAREHOLDERS.COM (Sept. 9, 2013, 9:23AM), http://kodak.boards.net/thread/6540/learned.

Similarly, another Eastman Kodak Company shareholder summarized her experience during the Chapter 11 bankruptcy thusly: "COMPLETE frustration, exasperation," remarking that she should have known better.[335] Reflecting upon her attempts to gain influence in the proceedings, she mused, "It was the old boys network hard at work. I was out of my league."[336] Further reinforcing the view that the individual common shareholders who participated in the case were not simply hoping to be made whole, this respondent was fully prepared to acknowledge that the company was no longer worth as much as it had been in its heyday: "[T]here was value there. My shares were worth at least .50 a share at the time."[337] This valuation estimate is, of course, a far cry from the company's $90 trading range in better days.[338]

In sum, the Eastman Kodak Company shareholders I encountered do not merely shoulder the disappointment of their substantial investment losses and any additional expenses they incurred in their self-advocacy efforts. They must also grapple with their deeply held belief that the legal system failed them. Many of the shareholders have largely integrated and moved on from the former, but have not even begun to recover from the latter. The following Part strives to carry the torch on their behalf, recommending legal reforms that might help to make the system more equitable for future investors of publicly traded companies who someday find themselves unwitting parties in interest to a Chapter 11 bankruptcy case.

IV. Opportunities for Legal Reform

This Article reveals why and how individual common shareholders of large corporate debtors increasingly use grassroots organization and direct action to attempt to overcome both their pronounced collective action obstacles and the effect of laws that systematically exclude them from the Chapter 11 negotiation table. At the same time, the analysis demonstrates how these mobilization efforts are simply not enough to enable common shareholders with small holdings to gain a voice in Chapter 11 proceedings and negotiate for better treatment. Without a seat at the negotiation table, it is extremely difficult for them to successfully advance arguments or bargain to receive a distribution. In effect, they are preemptively crammed down. Therefore, legal interventions are needed to address shareholder disenfranchisement and restore fairness in Chapter 11.

These reforms are important because, if shareholders are permitted to fully participate in the bankruptcy case, they will be better able to protect their substantive rights—such as by challenging questionable valuations and raising other arguments in the case—and perhaps even recover some value on account of their interests. While it is true that in some cases the settlements ultimately offered to shareholders on account of their equity interests

335. Interview with Nancy Bo (Jan. 2, 2014) (on file with author).

336. *Id.*

337. *Id.*

338. *See* Eastman Kodak Co. Annual Report (Form 10-K), at 18 (Mar. 11, 1998) (noting a high price per share for the first quarter 1997 of $94.75).

will be in violation of the absolute priority rule,[339] the mere prospect of such distributions in some cases should not justify the presumptive exclusion of an entire class of interest holders in all cases. In light of the pronounced collective action obstacles and other special challenges the debtor's widely dispersed common shareholders face,[340] bankruptcy law should tilt the scales back in their favor.

First and foremost, shareholders should have a seat at the bankruptcy negotiation table. As one conceivable solution, Congress could mandate the appointment of official equity committees instead of leaving the appointment within the discretion of the U.S. Trustee and the courts.[341] Of course, this solution has the potential to be overbroad. A mandate of this sort would lead to the appointment of official equity committees even in those cases where the debtor is indisputably insolvent from the outset, such that creditors would clearly bear the costs of formal equity representation. Under these circumstances, an equity committee would only further deplete what little remains of the bankruptcy estate, while contributing additional uncertainty to the process.[342]

In lieu of mandating the appointment of official equity committees in *all* cases, Congress could essentially overrule *Williams* by directing the U.S. Trustee and the bankruptcy court to entirely disregard the debtor's solvency when determining whether to appoint an official equity committee. Instead, the decision to appoint an official equity committee would be made based upon the *nature* of the restructuring. For instance, Congress could mandate the appointment of official equity committees for all Chapter 11 cases other than those that feature liquidating plans. Presumably, the potential for manipulation of valuation data is the highest in public company cases that contemplate that the historic shareholders will be wiped out and that other stakeholders will succeed to the equity position in the reorganized company.[343] These are also the cases in which shareholders are most likely to believe that they are being exploited, and where shareholder collective action obstacles are the greatest. This reform would go a long way towards fortifying shareholder rights, at the same time alleviating all parties from the burden of adjudicating the solvency question at the commencement of the case for the narrow purpose of determining whether to appoint an official equity committee. Of course, in many reorganization cases, the debtor will be hopelessly and indisputably insolvent, such that the ongoing involvement of an official equity committee would constitute a clear drain on the estate. In such cases, Professors LoPucki and Whitford's proposal for a preemptive cram down—with its attendant limitations and safeguards—would be an effective way to

339. We can assume such payments would be similar to those identified in a sample of 43 large commercial bankruptcy cases studied by LoPucki & Whitford, *supra* note 79, at 143–58 (documenting the relatively small settlements received by shareholders on account of their equity interests).

340. *See, e.g.*, S. REP. NO. 95-989, at 5796 (1978) (explaining that there is a "natural tendency of a debtor in distress to pacify large creditors with whom the debtor would expect to do business at the expense of small and scattered public investors").

341. A revision of this sort would be codified in 11 U.S.C. § 1102. Instead of providing only for the discretionary appointment of official equity committees, the statute would read as follows: "the United States trustee shall appoint a committee of creditors holding unsecured claims and a committee of equity security holders."

342. LoPucki & Whitford, *supra* note 53, at 706 (highlighting the various forms of mischief that official committees can introduce to a corporate restructuring).

343. *See generally* O'Rourke, *supra* note 29, at 414–27.

alleviate some of the burden by extinguishing the official equity committee's role in the case.[344]

As the least radical alternative, discretion to appoint an official equity committee may continue to reside in the U.S. Trustee and the bankruptcy courts, with the debtor's solvency still part of the analysis. But Congress or the courts ought to reject the *Williams* line of reasoning and return to a more shareholder-friendly standard governing the appointment of official equity committees in Chapter 11 cases.[345] Moreover, rather than forcing shareholders to engage in the impracticable task of putting forth their own valuation case, Congress or the courts could make it clear that shareholders need only raise a colorable claim that it cannot be determined at the commencement of the bankruptcy case whether the debtor is in fact balance sheet insolvent.[346] When considering shareholder requests for an official equity committee, bankruptcy courts should be required to view the evidence and draw reasonable inferences therefrom in the light most favorable to shareholders. In practical terms, given that the debtor's financial disclosures are typically riddled with caveats that the information may be incomplete, inaccurate, or misleading, such a standard would force the debtor who wishes to exclude shareholders from the negotiation table to stand by its disclosures. By essentially erring on the side of shareholders, such a standard would more fully take into account the unique collective action obstacles shareholders of large, publicly traded corporations face, as well as their inability to rely upon reimbursement of costs and expenses from the bankruptcy estate.

Of course, all of this sidesteps an even more fundamental problem. The appointment of an official equity committee may not be enough to meet the needs of the special class of equity security holders that is the subject of this Article: a publicly traded debtor company's widely dispersed individual common shareholders. Because the largest interest holders typically comprise official committees,[347] such committees are subject to capture by dominant shareholders who are likely to have their own divergent and even conflicted interests in the restructuring. Thus, in all cases, including those where an official equity committee has been appointed, as well as those that involve hopelessly insolvent debtors, Congress should authorize the appointment of a special committee or designated trustee to represent the individual common shareholders' interests.[348] This committee or trustee would possess more limited rights to examine the debtor and engage in plan negotiations but would nonetheless serve a vital role by communicating with individual shareholders, responding to their requests for information and support, and monitoring official committees that purport to advance shareholder interests. At the very least, one or more of

344. LoPucki & Whitford, *supra* note 79, at 187–89; LoPucki & Whitford, *supra* note 113, at 625.

345. In other words, Congress could expressly codify the standard for appointing official equity committees in the text of 11 U.S.C. § 1102. Or appellate courts—including potentially the Supreme Court—could weigh in, such as to overturn *Williams* and its progeny as well as mandate the application of a more lenient standard.

346. In *Eastman Kodak*, individual common shareholders seem to have clearly met this standard, demonstrating, among other things, that the debtor's financial statements relied on book values and excluded a host of vital assets.

347. *See* 11 U.S.C. § 1102(b)(2) (providing that the committee should generally be comprised of persons holding the "seven largest amounts of equity securities of the debtor of the kinds represented on such committee").

348. This position could be modeled after that which is proposed in Alces, *supra* note 37 (exploring the collective action obstacles shareholders of large corporations face and proposing an "equity trustee" to better represent their interests).

the U.S. Trustee offices, the bankruptcy courts, or the SEC should develop a division that specifically focuses on interfacing with public investors of Chapter 11 debtor corporations so that their interests are protected in the restructuring process. Special care should also be taken to ensure that more powerful investors do not take advantage of these resources by engaging in so-called "astroturfing"[349] to make it seem that more sympathetic shareholders drive their actions.

These procedural reforms would go a long way towards improving the position of shareholders of bankrupt companies and alleviating some of the structural strain inherent in Chapter 11's process.[350] But they are also only the tip of the proverbial iceberg. Indeed, as I have argued earlier, Chapter 11 suffers from a number of inequities and inefficiencies.[351]

In particular, Congress and bankruptcy courts should reconsider the system's reliance on negotiated settlements among dominant parties, as consensus-based and market-based processes often do nothing more than give powerful actors with existing market power the opportunity to control case outcomes.[352] And if shareholders—or any other major corporate claimants or interest holders—are systematically denied a seat at the bankruptcy negotiation table, then the purported reliance on consensus or market-based mechanisms to resolve corporate financial distress may be merely illusory. In essence, it may be a convenient legal fiction that obscures a far less palatable reality.

Congress and the bankruptcy courts should also reassess how Chapter 11 values debtor corporations.[353] Notwithstanding courts' recognition that GAAP ought not to be determinative of the debtor's solvency,[354] financial disclosures and solvency determinations in large commercial bankruptcies continue to rely on these and other prevailing financial reporting principles. As one possible fix, Congress or the courts could

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349. *See generally* Gabriel H. Markoff, *The Invisible Barrier: Issue Exhaustion as a Threat to Pluralism in Administrative Rulemaking*, 90 TEX. L. REV. 1065 (2012) (addressing the risks of so-called "astroturfing," concealing the true advocates of a particular cause of action by making it seem as though it originates from grassroots activists).

350. *See supra* note 30 and accompanying text (detailing the structural strain that underlies the commercial bankruptcy process).

351. *See generally* Dick, *supra* note 14 (arguing that stakeholders with existing market power take control of the bankruptcy restructuring process at the expense of other stakeholders); Dick, *supra* note 28 (making a similar claim and demonstrating how powerful stakeholders are able to extract excess returns).

352. *See* Dick, *supra* note 14 (addressing inequalities of the reorganization process).

353. In fact, in a recent survey of members of the American Bankruptcy Institute's Business Reorganization Committee, "[m]ost respondents . . . agreed with the following statement: 'Additional disclosures made by the debtor earlier in the case regarding . . . asset valuation would help facilitate more effective restructurings." Dalié Jiménez, *ABI Chapter 11 Survey Results*, 33 AM. BANKR. INST. J. 10, 11 (2014).

354. The Ninth Circuit eloquently captured the tension between GAAP and bankruptcy law in declaring that "[t]he authorities cited by the debtor do not compel the conclusion that the bankruptcy court must follow GAAP in making solvency determinations. Requiring application of GAAP would make accountants and the board which promulgate GAAP the arbiters of insolvency questions. Clearly the Code provides that judges should make such decisions. Furthermore, there is no policy reason why judges should not be allowed to consider subsequent events such as the actual collection rate for receivables, in valuing assets and determining liabilities. Thus although GAAP are relevant, they are not controlling in insolvency determinations." *In re* Sierra Steel, Inc. v. Totten Tubes Inc., 96 B.R. 275, 278 (9th Cir. 1989).

mandate that an independent, court-appointed examiner revalue the debtor's assets at fair market value at the commencement of a Chapter 11 case.

Of course, critics will likely argue that such a move would bring us back to the pre-1978 system of commercial restructuring, where cases often became mired in valuation battles. For those who prefer to place their trust in market mechanisms, the present system at least superficially seems to offer efficient outcomes.[355] But this assurance, while elegant in its simplicity, ignores a glaring problem: the debtor's valuation is not only a highly negotiated basis for ultimately distributing value, it is also presently the legal basis for inviting corporate constituencies to the negotiation table in the first place. Under the prevailing standard, shareholders cannot access the negotiation process at all unless they meet their burden of proving the debtor's solvency. For this reason, if the debtor's valuation is to remain a factor in the analysis, courts must take a more active role in determining valuation at two critical junctures: (1) at the commencement of the case, when parties are initially invited to the negotiation table, and (2) at plan confirmation, when value is ultimately distributed to claimants.

The estate's costs of adequately representing shareholders are, obviously, a concern. But the administrative burden has not prevented other parties from solidifying their own seats at the negotiation table. As Eastman Kodak Company shareholders observed early in the case, "in extremely large cases . . . the debtors, secured lenders and the official creditors' committee each hire highly expensive counsel, investment bankers, financial and other advisors," including "the most highly-regarded, and most expensive, law firms in America."[356] Accordingly, "none should be heard to complain that an Official Equity Committee will become an overwhelming administrative burden on the estates. Under this record, the contention is insincere."[357] Bankruptcy law must also take into account the broader social costs of systematically excluding a vital corporate constituency. Opportunities for abuse exist wherever persons are authorized to make decisions that impact others' interests without meaningful checks and balances. The fact that modern commercial restructurings are large and complex with the potential to be expensive and time consuming is no justification for continued reliance on a system that so ignores this basic axiom.

V. CONCLUSION

This Article's view of commercial restructurings under Chapter 11 is not particularly favorable. Although the Bankruptcy Code's drafters expressed a hope that a commercial debtor's equity investors would have access to formal representation in Chapter 11 cases,[358] corporate and bankruptcy laws have evolved in such a way that the debtor's non-

355. This is because when parties who are sensitive to transaction costs are encouraged to reach a negotiated settlement as to the debtor's valuation, they will presumably settle upon a calculation that—although not necessarily perfectly accurate—comes as close to the economic reality as rational actors would tolerate.

356. Kodak S'holders' Joint Motion, *supra* note 84, at 20. The shareholders highlight the large fees promised to certain of these professionals, "including monthly fees of $250,000, a guaranteed transaction fee of $12.5 million, and opportunities to generate other substantial incremental fees." *Id.*

357. *Id.*

358. *See supra* notes 144–146 and accompanying text (discussing the Senate report for the Bankruptcy Reform Act of 1978).

insider common shareholders are now largely excluded from the negotiation table.[359] Notwithstanding the *Williams* court's reassurances,[360] shareholders are unable to rely on the extant legal structures to protect their interests. As a result, they must engage in direct action and grassroots organization, often incurring significant personal costs. Even then, bankruptcy courts can simply choose to block their efforts on the grounds that they must be sore losers in an otherwise fair investment game. In other words, individual common shareholders can overcome their collective action obstacles, but they cannot overcome the legal barriers to full and meaningful participation in the case. Without a meaningful voice in the proceedings, they are, essentially, crammed down from the case's outset.

As it stands, Chapter 11's commercial restructuring process erodes public faith in the financial markets. Notwithstanding a dominant economic efficiency paradigm, the bankruptcy estate's costs of granting meaningful representation cannot justify the continued disenfranchisement of the debtor's public investors. This is especially true in cases contemplating that other stakeholders will succeed to the equity position in the reorganized company. If for no other reason than to help restore the financial markets' integrity in times of corporate financial distress, shareholders must have a meaningful opportunity to participate in Chapter 11 restructurings.

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359. *See supra* Part II (discussing the failure of traditional legal structures to promote shareholders' interests).

360. *See supra* note 210 and accompanying text (articulating the court's confidence that shareholders would be represented in the restructuring even without an official equity committee).

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