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Unwritten Rules and the New Contract Paradigm

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The emergence of large-scale corporate reorganization in the second half of the nineteenth century was the single most remarkable achievement of the common law in America. When a large railroad failed, as they often did, everyone wanted it to be reorganized.[1] All of the stakeholders would be worse off if the railroad was liquidated, even the senior creditors, since a mortgage on, say, a hundred miles of railroad track in the middle of nowhere was worth little if the railroad was shut down. The public interest also cried out for reorganization, given the growing nation's need for an effective system of transportation. Unfortunately, serious constitutional obstacles made it difficult for either Congress or the states to intervene. The courts filled the gap by giving their imprimatur to a remarkable innovation that became known as equity or railroad receivership. Creditors asked for a receiver and pretended to foreclose on the railroad's assets, but the parties actually reorganized the railroad through a "sale" that effected a restructuring of its obligations.

In the standard historical account, corporate reorganization evolved from this cobbled together, fast-and-loose process to a more formal, structured judicial proceeding. After decades of equity receivership practice, the story goes, Congress finally codified large scale corporate reorganization in the early 1930s.[2] Congress adopted sweeping reforms in 1938 and again in 1978, when current chapter 11 was put in place.[3] We now have an elaborate statute governing the reorganization of large troubled corporations.

In this Essay and the larger book from which it comes, Douglas Baird contends that the standard account misses an essential feature of corporate reorganization practice.[4] Corporate reorganization continues to take place through negotiations between the debtor and its creditors, just as it did over a

* S. Samuel Arsht Professor of Corporate Law, University of Pennsylvania. Thanks to Douglas Baird, Sarah Borders, Richard Levin, and Bruce Markell for helpful comments and conversation, and to the editors of the Emory Bankruptcy Developments Journal for including me in this fine symposium.

1 With apologies for immediately succumbing to the commenter's temptation to veer into self-reference, the events in this paragraph are described in detail in DAVID A. SKEEL, JR., DEBT'S DOMINION: A HISTORY OF BANKRUPTCY LAW IN AMERICA (2001).

2 *Id.* at 16.

3 *Id.* at 19.

4 Douglas G. Baird, *The Fraudulent Conveyance Origins of Chapter 11: An Essay on the Unwritten Law of Corporate Reorganizations*, 36 EMORY BANKR. DEV. J. 693 (2020); DOUGLAS G. BAIRD, THE UNWRITTEN LAW OF CORPORATE REORGANIZATIONS (unpublished manuscript, 2020).

century ago. These negotiations are governed by unwritten rules that "are well-known to insiders, but largely invisible to those on the outside."[5] The parties are expected to provide full disclosure, and to give robust participation rights to every affected party. Senior creditors can use modest payoffs to quiet potential objectors, but "other sorts of side deals are out of bounds."[6] The role of the judge is to serve as a vigilant referee, intervening if one of the players violates these unwritten rules.[7]

According to Professor Baird, the unwritten rules date back to the prohibition of actions that "hinder, delay, or defraud" in the statute of 13 Elizabeth nearly five hundred years ago.[8] Some of the unwritten rules, such as the insistence on full disclosure, have remained constant through time. In other respects, they have evolved. The unwritten rules, not bankruptcy's distribution rules or other features of the Bankruptcy Code (Code), are the essence of corporate reorganization. My colleague Charles Mooney once insisted that bankruptcy law is simply Civil Procedure.[9] For Professor Baird, bankruptcy's essence is fraudulent conveyance.

Professor Baird's story is highly persuasive, in my view, and captures a key dimension of bankruptcy practice that has not been fully appreciated. Even when Professor Baird is covering familiar ground, such as the emergence of equity receivership, he supplies new and interesting insights. Writing about early railroad receivership cases in which creditors of a subsidiary were given no recovery, for instance, Professor Baird discerns a logic to their exclusion: "the only ones given a seat at the bargaining table were those stakeholders who were to be part of the business going forward."[10] "[T]hose who had invested in the assets of the railroad that were to stay with the business" needed to be included, and to be given a recovery.[11] Others did not.

The story covers a great deal of ground very quickly, and as a result

[5] Baird, *Origins, supra* note 4, at 693.

[6] *Id.*

[7] "Rather than a dispenser of Solomonic wisdom, the bankruptcy judge is like a referee. A good referee ensures that the rules of the game are followed." *Id.* It is heartening that Professor Baird can unselfconsciously describe bankruptcy judges as "referees." Even a decade or two ago, the memory of the inferior status of "bankruptcy referees" under the old Bankruptcy Act was still fresh, and scholars would have avoided the referee metaphor.

[8] *Id.* at 693. In his comments on Professor Baird's essay, Professor Markell argues for much earlier origins. Bruce A. Markell, *Lawyers, Judges and Unwritten Rules*, 36 EMORY BANKR. DEV. J. 713 (2020).

[9] Charles Mooney, *A Normative Theory of Bankruptcy Law: Bankruptcy as (is) Civil Procedure*, 61 WASH. & LEE L. REV. 931 (2004).

[10] Baird, *Origins*, *supra* note 4, at 700.

[11] *Id.*

oversimplifies at times. The historical evolution also is bumpier than Professor Baird suggests. Rather than simply introducing more vigilant judicial oversight of the restructuring process,[12] for instance, the New Deal reformers seem to me to have sought and temporarily achieved a sharp break from prior practice. But the persistence of a handful of evolving implicit principles over many generations is remarkable, and quite revealing of how large-scale corporate reorganization actually works.[13] This project is the crowning achievement (so far, at least!) of the most important bankruptcy scholar of our time.

In the discussion that follows, I make two simple points. In the first part, I argue that what's good for bankruptcy insiders is not always good for everyone; in the second and third, that bankruptcy's written rules—by which I mean both statutory provisions and the parties' contracts—still matter, and they matter a lot.

I. THE DANGERS OF UNWRITTEN RULES

Professor Baird tells a (mostly) happy story about insolvency lawyers devising pragmatic solutions to financial distress under the benign but alert eye of judges who leave the parties to their own devices so long as they honor the unwritten rules. Although Professor Baird does not fully delineate them—perhaps because doing so would lift the lid on their mystery—the unwritten rules seem to include an expectation of full disclosure, a commitment to ensuring that everyone gets to participate, and an acceptance of "tips" but not bribes.

The foil in Professor Baird's story is bankruptcy's distributional rules, especially the absolute priority rule. The absolute priority rule is extolled by many as the essence of corporate reorganization. This view is mistaken in two respects, in Professor Baird's view. Not only does the conventional wisdom exaggerate the import of the distributional rules, but absolute priority is not even the best baseline. The first of these contentions is central here, and the second is developed in detail in Professor Baird's other work.[14]

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12 "The judge had to apply the principles of the Statute of 13 Eliz. c. 5 more aggressively, insist on full disclosure, and be quick to act if the potential for advantage-taking arose." *Id.* at 705.

13 Or, we might say, how reorganization and sales work. With respect to current chapter 11 cases, Professor Baird's discussion often seems more relevant to filings that lead to bankruptcy sales than to traditional reorganizations.

14 Professor Baird's doubts about absolute priority seem to have emerged in articles such as Douglas G. Baird & Robert K. Rasmussen, *Control Rights, Priority Rights and the Conceptual Foundations of Corporate Reorganizations*, 87 VA. L. REV. 921 (2001). His work has spawned a major debate on the priority question. *Compare* Douglas G. Baird, *Priority Matters: Absolute Priority, Relative Priority, and the Costs of Bankruptcy*, 165 U. PA. L. REV. 785 (2017); Anthony J. Casey, *The Creditors' Bargain and Option Preservation: Priority in*

While bankruptcy's unwritten rules are attractive in many respects, it is important to acknowledge the potential dangers of a non-transparent, insider-run system. In the early decades of the last century, the New Deal reformers thought that insiders' temptation to favor their own interests poisoned the entire reorganization process.[15] William Douglas famously condemned the "degeneration of the bar" in many reorganizations, and complained that "[c]onflicts of interest have had their corroding influence."[16] The voluminous report produced by the Securities and Exchange Commission under Douglas's guidance in the late 1930s repeatedly condemned the reorganization insiders who operated according to their own unwritten rules.[17]

The New Dealers' complaints were seasoned with hyperbole, in my view, but the temptation for insiders to favor their own interests, whether consciously or unconsciously, is real. The most obvious example is the fees charged by lawyers and bankers in large cases.[18] Because the leading players are repeat players, and will continue to work with one another in future cases, they have little incentive to police one another's compensation.[19] The principal current corrective in recent cases has been to appoint a fee examiner,[20] but even the most savvy fee examiner is only a limited substitute for policing by the parties who are most intimately involved in the case.

Chapter 11; 78 U. CHI. L. REV. 759 (2011); Anthony J. Casey & Edward R. Morrison, *Beyond Options* (working paper); *with* Barry A. Adler and George Triantis, *Debt Priority and Options in Bankruptcy: A Policy Intervention*, 91 AM. BANKR. L.J. 563, 583 (2017) (defending absolute priority).

15 Although my focus here is on large scale reorganization, bankruptcy cases involving smaller firms were thought to be controlled by "bankruptcy rings" for much of the twentieth century. A principal objective of the 1978 Code was to curb these abuses.

16 WILLIAM O. DOUGLAS, DEMOCRACY AND FINANCE 233 (James Allen ed., 1940).

17 "Managements and bankers seek perpetuation of [their] control for the business patronage it commands . . . ." the initial volume of the report contended. I SECURITIES AND EXCHANGE COMMISSION REPORT ON THE STUDY AND INVESTIGATION OF THE WORK, ACTIVITIES, PERSONNEL, AND FUNCTIONS OF PROTECTIVE AND REORGANIZATION COMMITTEES 863 (1937). Reorganization lawyers were no better: "The vice of the bar is that the bar has been charging all that the traffic will bear." *Id.* at 867.

18 Whether the fees are excessive is the subject of a longstanding debate. *Compare* LYNN M. LOPUCKI & JOSEPH DOHERTY, PROFESSIONAL FEES IN CORPORATE BANKRUPTCIES: DATES, ANALYSIS AND EVALUATION (2011) (contending that professional fees are excessive), *with* Stephen J. Lubben, *Corporate Reorganization & Professional Fees,* 82 AM. BANKR. L.J. 77 (2008) (more sanguine view of fees). Either way, they are enormous in many big cases, *see* Katy Stech Ferek, *Fed Says Lehman Brothers Chapter 11 Case is Costliest in History*, WALL ST. J. (Jan. 16, 2019) (discussing Federal Reserve projection that the fees and expenses in the Lehman Brothers bankruptcy will reach nearly $6 billion).

19 Fee examiners mitigate this problem to some extent, but imperfectly. *See, e.g.*, Stephen J. Lubben, *What We "Know" About Chapter 11 Cost is Wrong*, 17 FORDHAM J. CORP. & FIN. L. 1 (2012).

20 Another of the commentators on Professor Baird's essay, Professor Markell, is the fee examiner in the PG&E bankruptcy. *See, e.g.*, Alex Wolf, *PG&E Professionals, Examiner at Odds Over Non-Work Travel Fees*, BLOOMBERG LAW (Oct. 25, 2019), https://news.bloomberglaw.com/bankruptcy-law/pg-e-professionals-examiner-at-odds-over-non-work-travel-fees.

A more subtle version of the temptation to favor insiders is the tendency of bankruptcy professionals, and even bankruptcy judges, to privilege bankruptcy over alternative forums for resolving financial distress. This bias is one possible explanation for bankruptcy judges' more favorable response to restructuring support agreements (RSAs) and other contracts entered into during bankruptcy, than to intercreditor agreements that predate the bankruptcy filing. RSAs are drafted by bankruptcy professionals and increase the likelihood of a successful reorganization; intercreditor agreements are not and often do not.[21] To be sure, the preference for bankruptcy is not always undesirable. For instance, contracts made before bankruptcy sometimes have problematic features. However, bankruptcy courts appear to be excessively hostile to prebankruptcy contracts.[22]

A process that depends on negotiations among insiders also may also produce significantly suboptimal results. Professor Baird notes that "[w]hile there [are] many possible deals" in this environment, "the players naturally gravitate[] toward only a few"—a limited number of "focal points."[23] This can be beneficial if the focal points are likely to effectively resolve the debtor's financial distress. But what if the focal points are more problematic? If the focal points are major creditors' current claims, for instance, the restructuring may not be sufficiently robust, and the debtor may still have too much debt when it emerges from bankruptcy. This may have been a problem with railroad reorganizations a century ago,[24] and it could still be a problem in large-scale corporate reorganizations today.[25]

I do not think the dark sides of a process governed by unwritten rules are so dire that bankruptcy law needs to be completely upended. But I do think it is important to look for opportunities to diminish the distortions that attend a system run by insiders.[26]

[21] Bankruptcy insiders also can be expected to lobby for expansions of bankruptcy, and to resist other incursions on their territory, such as efforts by the parties to waive bankruptcy.

[22] *See, e.g.*, Kenneth Ayotte, Anthony J. Casey, & David A. Skeel, Jr., *Bankruptcy on the Side*, 112 NW. U. L. REV. 255, 257–58 (2017) (criticizing courts' use of a "clear beyond peradventure" standard in policing intercreditor agreements).

[23] Baird, *Origins*, *supra* note 5, at 710 n.83. (citing THOMAS C. SCHELLING, THE STRATEGY OF CONFLICT 57–58 (1960)).

[24] *See* Stephen Lubben, *Railroad Receiverships and Modern Bankruptcy Theory*, 89 CORNELL L. REV. 1420, 1449 (2004).

[25] Mark Roe made this argument decades ago. *See* Mark J. Roe, *Bankruptcy and Debt: A New Model for Corporate Reorganization*, 83 COLUM. L. REV. 527 (1983).

[26] In response to somewhat analogous concerns in corporate law—plaintiffs' lawyers challenges to nearly every large proposed merger—Delaware has cracked down on disclosure-only settlements. *See In re* Trulia, Inc. Stockholder Litigation, 129 A.3d 884, 898–99 (Del. Ch. 2016) (requiring proponents of a disclosure-only settlement to show the disclosures are "plainly material").

II. THE WRITTEN RULES MATTER

The great insight of Professor Baird's essay is demonstrating just how much a simple set of unwritten principles matter, and tracing them back to early fraudulent conveyance law. These principles are indeed central—much more central than anyone realized before Professor Baird's work-- but it is important to recognize just how much the written rules still matter.[27]

Fraudulent conveyance law itself nicely makes this point. Professor Baird focuses on the early emergence of fraudulent conveyance law, which prohibited intentional misbehavior by debtors and came to rely on a loose set of "badges of fraud."[28] In its traditional garb, fraudulent conveyance law depends more on standards than on rules. But it has become increasingly rules oriented, thanks to the widespread adoption of "constructive fraud" statutes in the early twentieth century. If an insolvent debtor transfers property for less than reasonably equivalent consideration, the transfer can be avoided.[29] Although "constructive fraud" is something of an oxymoron, as Charles Tabb has aptly pointed out,[30] it now figures far prominently than the traditional, "actual" fraud provisions, in no small part because it is rule-oriented and easy to apply.[31] To be sure, discretion comes into play at times even with constructive fraud, but its use is rarely determined by the "unwritten rules."

Bankruptcy's distributional rules also seem more consequential than Professor Baird's story allows. Under the flexible version of absolute priority in current law, the rules serve as a backstop to the parties' efforts to negotiate a restructuring. A class of creditors can agree to treatment that violates the absolute priority rule.[32] If the class votes no, however, the proposed plan cannot be confirmed if it deviates from the absolute priority rule with respect to that class.[33]

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[27] Richard Levin also emphasizes the importance of the written rules in his commentary—an especially appropriate perspective given that he was one of the principal drafters of the Bankruptcy Code. Richard Levin, *A Response to Professor Baird's Essay on Unwritten Law*, 36 EMORY BANKR. DEV. J. 723 (2020).

[28] "*Twyne's Case* held that, in addition to transactions involving actual fraud, the Statute of 13 Eliz. empowered the court to strike down any transactions that had 'badges of fraud.'" Baird, *Origins*, *supra* note 4, at 694.

[29] Professor Baird hints at this feature of modern fraudulent conveyance law, but it does not figure in the unwritten rules. *Id.*

[30] CHARLES JORDAN TABB, THE LAW OF BANKRUPTCY 591–92 (2d ed. 2009).

[31] Preference law is now similarly rule-oriented, as Professor Baird notes. Baird, *Origins*, *supra* note 5, at 696 n.21 (citing Robert Weisberg, *Commercial Morality, the Merchant Character, and the History of Voidable Preference*, 39 STAN. L. REV. 3, 4–5 (1986)).

[32] *See* 11 U.S.C. § 1129(a)(8) (2019).

[33] *See* § 1129(b).

Professor Baird does acknowledge that the distributional rules perform a useful function by forcing the debtor to give every major class a seat at the bargaining table. Professor Baird suggests that this, rather than the rules themselves, is the principal contribution of priority. "Protecting the bargaining environment rather than ensuring proper division of the assets is the task at hand[,]" he writes.[34] "Ensuring that distributional rules are followed is necessary to do this and hence a necessary part of ensuring that the players follow the rules of the game, but it is hardly the only part."[35]

The seat-at-the-table benefit of the priority rules does seem essential, but the priority rules strike me as doing more than this alone. In my view, the absolute priority rule provides an essential baseline for the bankruptcy process.[36] One of the difficulties of the unwritten rule that modest payments to potential dissenters are okay but side payments and bribes are not is that it is extraordinarily difficult to tell which is which. In its much-discussed *Jevic* decision, the Supreme Court, perhaps in part for this reason, adopted a per se prohibition against payments that bypass a higher priority class in the context of a so-called structured dismissal.[37] The absolute priority rule does not just force the debtor and senior creditors to permit the intervening party to participate; it prohibits them from implementing a plan—no matter how compelling the plan may seem—that does not honor the intervening party's priority rights.

One context where the unwritten tip-versus-bribe rule does still operate is when a senior creditor that may have a claim to all of the debtor's assets purports to redirect some of its recovery to a lower priority class. In an asset sale, this takes the form of a "tip" to the creditors committee. In a traditional reorganization, it takes the form of a "gift" from senior creditors to one class of lower priority class of claims but not others. Whereas courts have often allowed tips in the sale context, with traditional reorganizations, the principal focus of Professor Baird's essay, courts (especially appellate courts) have been quite hostile, often insisting on adherence to bankruptcy's written rules.[38] It is possible that one reason tips are more prevalent than gifts is that it is nearly impossible for an objecting creditor to challenge an asset sale that has been negotiated by insiders and approved by the bankruptcy judge, due to a strong statutory

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34 Baird, *Origins*, *supra* note 4, at 709.

35 *Id.*

36 It is also worth noting that the choice of priority rule can significantly affect the parties' incentives and the bargaining dynamics.

37 *See* Czyzewski v. Jevic Holding Corp., 137 S. Ct. 973, 986–87 (2017).

38 *See, e.g.*, Dish Network Corp. v. DBSB N. Am., Inc. (*In re* DBSD N. Am., Inc.), 634 F.3d 79, 98, 100 (2d Cir. 2011); *In re* Armstrong World Indus., Inc., 432 F.3d 507, 512–13 (3d Cir. 2005).

presumption that sales will not be undone.[39] This may be a context where the written rules have the ironic effect of protecting decisions made in accordance with the unwritten rules.[40]

III. THE NEW CONTRACT PARADIGM

The place where Professor Baird's emphasis on unwritten rules and the continuing importance of written rules most fully come together is contract. The most dramatic development in recent reorganization practice is the extent to which reorganization cases are now shaped by pre-bankruptcy (ex-ante) contracts, and by contracts negotiated during the bankruptcy case (ex-post). Elsewhere, George Triantis and I have called this the new "contract paradigm."[41]

Contracts have always been central to large scale reorganization, of course. In a railroad receivership, investors "deposited" their securities with the committee negotiating on their behalf pursuant to a contract, and the committees joined together to form a reorganization committee pursuant to another contract.[42] But the scope of contract has dramatically expanded with respect to both prebankruptcy contracting and contracting during the bankruptcy case.

Start with prebankruptcy contracting. Financial contracting is far more sophisticated today than in earlier generations, which has dramatically expanded the range of potential prebankruptcy contracts. It is now possible to divvy up cash flows in ways that would have been unimaginable in the past, and to allocate responsibility in the event of financial distress. The new contracts include intercreditor agreements and unitranche arrangements, in addition to more traditional loan syndicates.[43]

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[39] *See* 11 U.S.C. § 363(m) (2019) (good faith sale cannot be reversed unless it is stayed pending appeal). It also is difficult to appeal bankruptcy judges' orders confirming a reorganization plan, due to equitable mootness doctrine. But equitable mootness is not as complete a barrier to challenge as § 363(m).

[40] There is a more general point here as well: the unwritten rules benefit from the difficulty of appealing decisions made at the bankruptcy court level. If existing constraints on appeal such as equitable mootness doctrine are relaxed, the unwritten rules could have less sway, at least on the margins. For criticism of current equitable mootness doctrine, *see* Bruce Markell, *The Needs of the Many: Equitable Mootness' Pernicious Effects*, 93 AM. BANKR. L.J. 377 (2019).

[41] David A. Skeel & George Triantis, *Bankruptcy's Uneasy Shift to a Contract Paradigm*, 166 U. PA. L. REV. 1777, 1780 (2018).

[42] "Various committees, generally organized by the management or underwriters of the securities, sprang up," as one mid-twentieth century commentator put it. "These committees without court supervision drew their own deposit agreements, solicited the deposit of securities and formulated plans of reorganization by negotiation and agreement among the various classes of security holders." Arthur H. Dean, *Corporate Reorganization*, 26 CORNELL L. Q. 537, 538 (1941).

[43] For an analysis of intercreditor agreements and proposals for policing them, *see* Skeel, et al., *Bankruptcy on the Side*, *supra* note 22, at 258, 261.

Post-petition contracting also figures much more prominently than in the past. This is in part due to several underappreciated features of the 1978 Code itself. Unlike the earlier Bankruptcy Act, which constrained the scope of ex post contracting, the Code encourages the parties to renegotiate their entitlements through features such as the voting rules, which make the terms of a restructuring binding if the specified majority of a class approves, and the ability to wave off the absolute priority rule for any class that approves.[44]

Current bankruptcy law also has a second distinctive feature in this regard: it converts many stakeholders who did not have prebankruptcy contracts with the debtor into what are, in effect, contract creditors.[45] Tort victims, for instance, are given unsecured claims, which can be renegotiated in the same fashion as prebankruptcy contracts. Under prior bankruptcy law, many of these claims would not have been "provable," and as a result would not have been part of the bankruptcy case.[46] Nearly every pre-petition obligation against the debtor becomes a contract claim in bankruptcy.

More recently, another form of ex-post contracting has emerged. The parties in most large-scale reorganizations now enter into restructuring support agreements (RSAs) or plan support agreements (PSAs).[47] (Although the terms are sometimes used interchangeably, agreements negotiated prior to the bankruptcy filing are usually called RSAs and those that first emerge during the bankruptcy case PSAs). RSAs and PSAs are designed to bind the signatories to the terms of an anticipated reorganization plan. This can be particularly important if the debtor's claims are actively traded. In addition to imposing deadlines for confirmation of a reorganization plan and other key steps in the bankruptcy process, these contracts require each signatory to ensure that any purchaser of its claims will also be bound.[48]

Much more than the new ex-ante contracts, the new ex-post bankruptcy contracts are subject to the unwritten rules Professor Baird has identified. RSAs and PSAs often include fees that are designed to compensate signatories for their

[44] *See* Skeel & Triantis, *supra* note 41, at 1799–800.

[45] 11 U.S.C. § 101(5) (2019) (defining "claim" expansively, as any "right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured . . . .").

[46] *See, e.g.*, Stephen Allen Edwards, Note, *Tort Claims Under the Present and Proposed Bankruptcy Acts*, 11 U. MICH. J.L. REFORM 417, 418–24 (1978) (discussing the limits of "provability" for tort claims).

[47] *See, e.g.*, Edward Janger & Adam J. Levitin, *Badges of Opportunism: Principles for Policing Restructuring Support Agreements*, 13 BROOK. J. CORP. FIN. & COM. L. 169 (2019); Douglas G. Baird, *Bankruptcy's Quiet Revolution*, 91 AM. BANKR. L.J. 593 (2017).

[48] *See, e.g.*, David A. Skeel, Jr., *Distorted Choice in Corporate Bankruptcy*, YALE L.J. (forthcoming 2020).

role in negotiating a potential plan and to induce other signatories to sign.[49] The terms of the fees seem to reflect the leading bankruptcy professionals' understanding of the line between acceptable fees and illegitimate vote buying.

There are points of friction between both (ex-ante) intercreditor agreements and (ex-post) RSAs, on the one hand, and key provisions of the Code, on the other. Some intercreditor agreements appear to interfere with bankruptcy's voting rules, for instance, by assigning junior lienholders' voting rights to the senior lienholders or forbidding junior lienholders from challenging a plan supported by the seniors.[50] By committing signatories to vote in favor of an anticipated plan, RSAs and PSAs seem to violate the requirement that a disclosure statement be distributed before the debtor solicits votes.[51] Despite the similarity of the frictions, bankruptcy judges have been much more deferential to RSAs and other ex-post agreements than to ex-ante agreements. As noted earlier, this may in part be because ex-post agreements are negotiated by other bankruptcy insiders, in accordance with the insiders' code of context.[52] In my view, courts have been too hostile to ex-ante agreements and at times too deferential to ex-post agreements, with potentially detrimental effects for the efficiency of the large-scale reorganization process.[53]

The Eighth Circuit's recent *Peabody Energy* case is a good illustration.[54] A central issue when Peabody Coal filed for bankruptcy was a dispute over the scope of the senior lenders' liens. At the request of the debtor, the issue was submitted to mediation. Creditors who wished to participate in the mediation were required to refrain from claims trading during the process. Rather than simply resolving the lien dispute, the mediation led to a proposed reorganization plan. The principal participants in the mediation would have an exclusive right to participate in 22.5% of a private placement of preferred stock at a price 35% below the stock's expected value.[55] Any creditor could participate in the other two slices of the placement, but only if they signed a PSA reflecting the terms

49 *Id.*

50 *See* Bank of Am. v. N. LaSalle St. Ltd. P'ship (*In re* 203 N. Lasalle St. P'ship.), 246 B.R. 325 (Bankr. N.D. Ill. 2000) (contractual provision assigning junior creditors' votes to senior creditors).

51 *See* 11 U.S.C. § 1125 (2019).

52 *See supra* notes 21–22 and accompanying text.

53 Skeel & Triantis, *supra* note 41, at 1817. This does not mean there is no need to police intercreditor agreements and other ex-ante contracts. There is. Courts should be mindful, for instance, of potential externality effects on other creditors. Skeel, et al., *Bankruptcy on the Side*, *supra* note 22. But this does not require courts to ignore the contracts altogether or interpret them in highly uncharitable fashion.

54 Ad Hoc Comm. of Non-Consenting Creditors v. Peabody Energy Corp. (*In re* Peabody Energy Corp.), 933 F.3d 918 (8th Cir. 2019). For a more extensive discussion of the case, *see* Skeel, *Distorted Choice*, *supra* note 48.

55 *In re Peabody Energy Corp.*, 933 F.3d at 922.

of the proposed plan within 3 days for the second (5%) slice and within 30 days for the third (72.5%) slice.[56]

Although the terms of the private placement were deeply problematic, it was approved by the courts. The arrangement could perhaps be critiqued under bankruptcy's unwritten rules. If the entrance requirements for participating in the mediation were too onerous, the reasoning might go, the unwritten rule guaranteeing everyone a "seat at the table" was violated and the private placement should have been disallowed.[57] But this approach seems quite indirect. The real question is not whether everyone had an opportunity to participate; it is whether the contract should be enforceable as written, or whether its terms are problematic. This is the approach courts apply in corporate law and it seems to me the approach courts should apply here.[58] The more general point is that, while bankruptcy's unwritten rules are important, the central issue in current reorganization practice is managing the tradeoffs between ex-ante and ex-post contracting.

CONCLUSION

This Essay is the latest in a long line of path-breaking Douglas Baird writings. He has discovered a feature of the evolution of large-scale organization that other scholars were vaguely aware of, but whose importance no one had fully recognized. In this commentary, I have simply endeavored to put Professor Baird's insights into a larger context, by offering reminders that an insider-oriented system has downsides as well as benefits, and that the written law of bankruptcy still matters a great deal.

[56] *Id.*

[57] As Professor Baird posited in an email discussion among the participants on the panel for which this commentary was written. Email from Douglas G. Baird, Professor, The University of Chicago Law School, to author (Feb. 17, 2020, 4:46 p.m.) (on file with author). In my view, the requirement that mediation participants refrain from trading should not be viewed as an excessively onerous obligation, but I acknowledge this is debatable.

[58] In Paramount Commc'ns., Inc. v. QVC Network, Inc., 637 A.2d 828 (Del. 1993), for instance, the Delaware Supreme Court invalidated a lockup agreement, deeming its terms excessively generous to the bidder and likely to interfere with alternative bids for the target corporation.