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Chapter 11's Silver Bullet and the Search for Liquidity

Jonathan Goodelman*

I. INTRODUCTION

The failure of Lehman Brothers sent the global financial sector into complete disarray, which hastened the biggest global economic meltdown the modern world has ever seen. In order to prevent further catastrophe, the United States, through the Troubled Asset Relief Program (“TARP”), spent \$700 billion in taxpayer money to bail out banks after the financial crisis.¹ Congress responded to this highly controversial bailout and the demand for legislation by enacting the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act” or “Dodd-Frank”).² This legislation is put forth in order to address the idea that these institutions are “too-big-to-fail.”³

According to the Dodd-Frank Act’s title page, the statute’s purpose is “[t]o promote the financial stability of the United States by improving accountability and transparency in the financial system, to end ‘too big to fail,’ to protect the American taxpayer by ending bailouts, to protect consumers from abusive financial service practices, and for other purposes.”⁴ Particularly, Title II of the Dodd-Frank Act establishes the

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¹ Bob Ivory talk, *The True Cost of the Bank Bailout*, NEED TO KNOW ON PBS (Sept. 3, 2010), <http://www.pbs.org/wnet/need-to-know/economy/the-true-cost-of-the-bank-bailout/3309/>.

² See generally Jennifer Meyerowitz & Joseph N. Wharton, *A Dodd-Frank Living Wills Primer: What You Need to Know Now*, vol. XXXI, No. 7, AM. BANKR. INST. L.J. 34 (2012); see also Bruce Grohsgal, *Case in Brief Against*, “Chapter 14,” vol. XXXIII AM. BANKR. INST. L.J. 44 (2014).

³ Nizan Geslevich Packin, *The Case against the Dodd-Frank Act’s Living Wills: Contingency Planning Following the Financial Crisis*, 9 BERKELEY BUS. L.J. 29, 32 (2012) (defining “too-big-to-fail” as the “problem caused when certain multinational financial institutions are so large that their insolvency could shake the entire financial system and the economy”); see also Lawrence A. Cunningham, *Too Big to Fail: Moral Hazard in Auditing and the Need to Restructure the Industry before It Unravels*, 106 COLUM. L. REV. 1698, 1726–27 (2006) (explaining that the term “too-big-to-fail” has received a lot of attention in the last two decades).

⁴ 12 U.S.C. § 5301 (2012).

Orderly Liquidation Authority (“OLA”).⁵ The OLA is established to liquidate failing financial firms and simultaneously prevent the liquidation from disrupting the market place.⁶ Supporters of the OLA claim that taxpayer bailouts are a thing of the past because the Federal Deposit Insurance Corporation (“FDIC”) has now been given the power to place a failing financial firm within their receivership.⁷ Once in receivership, the FDIC winds the financial firm down efficiently and orderly without forcing taxpayers to foot the bill.⁸ Supporters argue because the FDIC can facilitate the liquidation without taxpayer funds, the “too-big-to fail” problem is relinquished.⁹ The presumption of ending the “too big to fail” phenomenon has sparked an active debate on whether it is wise to entrust another regulatory body (considering the Federal Reserves regulations did not prevent the failure), with the difficult task of resolving it, when the proper mode of resolution lies in the federal bankruptcy system.¹⁰

Bankruptcy is favorable to an OLA receivership because it allows for unassisted failure of a financial firm. Unassisted failure ensures that the government will not step in to bail out a financial firm in the event of distress. Furthermore, if a bailout is no longer an option, institutions are prevented from taking risks with the belief that they will be rescued in the event they face financial distress.¹¹ Moreover, by taking away the

⁵ Mark A. McDermott, *Analysis of the Orderly Liquidation Authority, Title II of the Dodd-Frank Wall Street Reform and Consumer Protection Act*, SKADDEN COMMENTARY ON THE DODD-FRANK ACT, July 2010 at 1 (“Title II of the Dodd-Frank Act, titled ‘Orderly Liquidation Authority,’ creates an entirely new insolvency regime for large, interconnected financial companies, including broker-dealers, whose failure poses a significant risk to the financial stability of the United States.”).

⁶ See generally *id.*

⁷ See generally Report prepared by the Republican Staff of the Committee on Financial Services, U.S. House of Representatives, *Failing to End Too-Big-To-Fail: An Assessment of the Dodd-Frank Act Four Years Later*, available at http://financialservices.house.gov/uploadedfiles/071814_tbtfr_report_final.pdf.

⁸ *Id.*

⁹ *Id.*

¹⁰ *Id.*

¹¹ *The Bankruptcy Code And Financial Institution Insolvencies: Hearing Before Subcomm. on Regulatory Reform, Commercial and Antitrust Law of the Comm. on the Judiciary H.R. , 113th Cong. 13-14*

expectation of support by the government, institutions will be more aware of the risks they are taking and are likely to borrow less.¹² The decrease in the use of borrowing leads to less use of short-term funding and excessive leverage. Accordingly, this leads to a reduced likelihood that a financial firm would need support in the first place.¹³

Despite the safeguards put in place by the Dodd-Frank Act, there remains the argument that after witnessing the bankruptcy of Lehman Brothers, the Bankruptcy Code, as it reads today, is not an effective mechanism to resolve the failing of a systemically important financial institution (“SIFI”).¹⁴ Even if the critics are correct about bankruptcy law not being capable of providing resolution, the new Dodd-Frank regime makes clear that the OLA is a last resort, not a first resort to the Bankruptcy Code. In a recent house subcommittee discussion on financial institution resolution, Jeffrey Lacker, president of the Federal Reserve Bank of Richmond, Va., noted that both “Titles I and II of the Dodd-Frank Act ‘clearly’ envision bankruptcy without government support as the ‘first and most preferable option’ in the case of a failing financial institution.”¹⁵ Lacker argues that if resolution in bankruptcy without government support becomes the norm, “the incentives of market participants would be better aligned with our public policy goal of a financial system that effectively allocates capital and risks.”¹⁶ As mentioned above, this leads to

(2013)[hereinafter *2013 House Hearing*] (statement of Jeffrey M. Lacker, President of the Federal Reserve Bank of Richmond).

¹² *Id.* (explaining that “the problem-widely known as “too-big-to-fail” consists of two mutually reinforcing expectations”).

¹³ *Id.*

¹⁴ 12 U.S.C. § 5464 (providing standards for systemically important financial market utilities and payment, clearing, or settlement activities); *see also* Investopedia, <http://www.investopedia.com/terms/s/systemically-important-financial-institution-sifi.asp> (“Any firm as designated by the U.S. Federal Reserve, whose collapse would pose a serious risk to the economy. Systematically important financial institutions became the target of legislation and regulatory reform by the Obama Administration, due to issues concerning their consolidated supervision and regulation, following the financial crisis of 2008.”).

¹⁵ *Legislative Highlights; House Subcommittee Discusses Financial Institution Resolution Through the Code*, AM. BANKR. INST. L.J., Jan.2014, at 10, 68.

¹⁶ *See 2013 House Hearing, supra* note 11, at 15 (statement of Jeffrey M. Lacker).

large financial firms wanting to be “less leveraged and less reliant on unstable short-term funding.”¹⁷ Hence, institutions and markets become resilient when faced with financial stress, and policy makers could credibly renounce the commitment to rescue distressed financial firms that potentially could disrupt the market place.¹⁸

With that in mind, this Comment examines how distressed financial firms can be resolved through the bankruptcy process without drawing on emergency government support, exemplified by the government bailout during the 2008 financial crisis. The bankruptcy process has long been favored as the primary mechanism for dealing with distressed and failing companies. Now has come the time that financial companies are subjected to the bankruptcy process as well. Bankruptcy should be favored as the primary mechanism for dealing with distressed and failing financial firms to deter reckless corporate decisions made in the penumbra of the bailout safety net, in lieu of bailouts. Applying bankruptcy principles such as impartiality, adherence to established precedent, and due process to failing financial firms sets a necessary bright-line standard to hold corporations fiscally responsible. However, the Bankruptcy Code is not without flaw, enforcement of a uniform and predictable Bankruptcy Code is needed. The goals of this Comment are to examine the current problems with the Bankruptcy Code, in particular, issues arising with Chapter 11’s ability to reorganize a distressed financial firm and to explore proposed changes to the Bankruptcy Code by way of the Financial Institution Bankruptcy Act of 2014 (“FIBA 2014”).

¹⁷ See 2013 House Hearing, *supra* note 11, at 15 (statement of Jeffrey M. Lacker).

¹⁸ See 2013 House Hearing, *supra* note 11, at 15 (statement of Jeffrey M. Lacker).

Moreover, this Comment takes the position that the “single point of entry” (SPOE)¹⁹ approach is the most viable and efficient method to resolve a distressed financial institution that is organized with a holding company atop the corporate structure. Through FIBA’s proposed amendment to the Bankruptcy Code, the SPOE approach can be put to work through the bankruptcy process. Additionally, this Comment argues that the proposed amendments allow the bankruptcy process to facilitate the orderly resolution of a financial firm, while minimizing negative effects to the financial markets (so-called systemic disruption), and protecting tax-payers from loss and maximizing value for stakeholders. Finally, this Comment determines that a bankruptcy-style resolution, even under a revised Bankruptcy Code could work without government funding; however, the process should be safeguarded by having the government as a lender of last resort.

Accordingly, Part II discusses why bankruptcy (particularly Chapter 11) is the preferred mechanism for resolution of systemically important financial firm. Part III addresses the current problems with the Bankruptcy Code. Part IV will discuss the proposed revisions made to the Bankruptcy Code by way of FIBA 2014. Part V considers the remaining problems in the Bankruptcy Code. Part VI concludes this Comment.

II. THE DODD-FRANK ACT AND THE PREFERENCE FOR BANKRUPTCY

State and federal government have always played a significant role in banking, and is the main reason why the bankruptcy process has taken a secondary role to federal bank regulators when it comes to handling their insolvency.²⁰ With the passage of the Dodd-Frank Act, regulators maintain their position in banking, despite the fact that the bankruptcy process has long been favored as the primary mechanism for dealing with

¹⁹ For a discussion on SPOE, *see infra* part IV.

²⁰ *See generally* Kimberly Anne Summe, LESSONS LEARNED FROM THE LEHMAN BANKRUPTCY, *in* ENDING BAILOUTS AS WE KNOW THEM 65–67 (Kenneth E. Scott et al. eds., Hoover Institution Press 2010).

distressed and failing companies.²¹ Bankruptcy is favored because of its impartiality, adherence to established precedent, and the fact that it is grounded in the principles of due process and rule of law.²² With the collapse of the financial sector in 2008, Congress had the opportunity to limit the divide between banking and bankruptcy and create a more unified system, but instead, pursuant to Title II of the Dodd-Frank Act, it created a new system for addressing financial distress. Despite a good faith attempt by Congress to establish an efficient and orderly resolution regime, the legislation has left gaps between bankruptcy resolution and the new federal resolution regime. But as this Comment will discuss, proposed changes to the Bankruptcy Code, by way of the FIBA 2014, allows for a regime integration that could narrow the gaps and provide a more unified system of resolution for a failing financial firm, which may account for both state and federal interests. This Comment will first discuss why bankruptcy is the preferred mechanism for resolution of a systemically important financial institution and why the Bankruptcy Code must be revised to work in sync with the Dodd-Frank Act.

The Dodd-Frank Act makes clear that the use of bankruptcy, not the OLA, is the preferred mechanism for resolution of SIFI.²³ The OLA is only used in limited situations, such as where bankruptcy is not a viable option because of the possible risks posed to the U.S. financial market.²⁴ The Dodd-Frank Act envisions bankruptcy as the preferred mechanism in two key places. The first being in Title I, with the instituting of a resolution

²¹ *Id.*

²² *Id.*

²³ See 2013 House Hearing, *supra* note 11, at 82-3 (statement of Donald S. Bernstein, co-chair of the Insolvency and Restructuring Group at Davis Polk & Wardwell LLP).

²⁴ FED. DEPOSIT INS. CORP., ADVISORY COMM. ON SYSTEMIC RESOLUTION: THE SINGLE POINT OF ENTRY RESOLUTION STRATEGY (2013).

plan, or so called “living will” under Section 165(d).²⁵ Under Title I, covered financial institutions are required to put forth a plan, subject to review by the Federal Reserve Board, the Financial Stability oversight Council, and the Federal Deposit Insurance Corporation that demonstrates how the financial institution will orderly resolve their affairs “in the event of material financial distress or failure”²⁶ under the Bankruptcy Code.²⁷ Essentially, because these resolution plans are tested in a bankruptcy proceeding, bankruptcy is seen to be the preferred mechanism of choice for a failing financial firm. Otherwise regulators would have required a financial firms plan to be tested under another mechanism, such as the OLA.²⁸ The fact that these resolution plans will be tested against bankruptcy validates the inference that it is “critically important to the development of credible resolution plans under Title I . . . that bankruptcy law is effective in its ability to resolve SIFI’s.”²⁹

The second point envisioning bankruptcy as the preferred resolution mechanism can be seen in the context of government regulators’ ability to initiate the actual OLA process.³⁰ In order for Title II to be invoked, government regulators must find that bankruptcy is wanting; therefore, “by its own terms, bankruptcy is designed by the Dodd-Frank Act to be the preferred resolution mechanism.”³¹ With the declaration of bankruptcy as the presumptive procedure for resolution, comes the necessity to equip the

²⁵ See generally *Corporate and Financial Institution Insolvencies: Hearing Before Subcomm. on Regulatory Reform, Commercial and Antitrust Law of the Comm. on the Judiciary H.R. 113th Cong.* 98 (2014) [hereinafter *2014 House Hearing*] (statement of Thomas H. Jackson, Distinguished University Professor & President Emeritus University of Rochester.)

²⁶ 12 U.S.C. §5301-165(d)(1) (2012); see also 12 U.S.C. § 5366 (d)(1) (2012).

²⁷ See generally Jennifer Meyerowitz & Joseph N. Wharton, *A Dodd- Frank Living Wills Primer: What You Need to Know Now*, AM. BANKR. INST. J., Aug. 2012, at 34. This looks correct to me according to rule 16.5

²⁸ See *2014 House Hearing*, supra note 25, at 99 (statement of Thomas H. Jackson).

²⁹ *Id.*

³⁰ *Id.*

³¹ *Id.*; see also Remarks by Martin J. Gruenberg, Chairman, Federal Deposit Insurance Corporation, on Implementation of the Dodd-Frank Act before the Volker Alliance Program (Oct. 13, 2013), available at <http://www.fdic.gov/news/news/speeches/spoet1313.html>.

Bankruptcy Code with the proper tools so that it may accomplish the goals of minimizing losses and placing them on appropriate, pre identified, parties; minimize systemic consequences; and prevent a government bail-out.³² Moreover, these goals are in line with the two goals of the Dodd-Frank Act: (1) limiting the risk of contemporary finance; and (2) reducing the damage caused by the failure of a large financial institution.³³

A. *Bankruptcy Is A Superior Resolution Mechanism.*

The OLA of Title II is an inferior alternative to the well-established legal landscape of bankruptcy for the simple reason that it “imbues the FDIC with unfettered discretion to exercise its orderly liquidation authority.”³⁴ Bankruptcy has an already-developed legal landscape and is administered by an impartial tribunal with clear rules in place.³⁵ Together, the clear rules administered by learned bankruptcy judges provide for the application of a uniform resolution regime that allows financial institutions to properly plan their “living will” under Title I in the event of an insolvency or financial crisis.³⁶

Despite the fact that the FDIC has announced that it supports the idea that bankruptcy, not the OLA, should be the presumptive resolution procedure, an ongoing debate still exists on whether the OLA is preferable to bankruptcy.³⁷ Supporters of the OLA argue that orderly liquidation is preferable to bankruptcy because bankruptcy

³² 2014 House Hearing, *supra* note 25, at 99–100 (statement of Thomas H. Jackson).

³³ See generally David Skeel, *THE NEW FINANCIAL DEAL: UNDERSTANDING THE DODD-FRANK ACT AND ITS (UNINTENDED) CONSEQUENCES* (John Wiley & Sons, Inc. 2011).

³⁴ James H.M. Sprayregen & Stephen E. Hessler, *Too Much Discretion To Succeed: Why A Modified Bankruptcy Code Is Preferable To Title II Of the Dodd-Frank Act*, FED. RES., http://www.federalreserve.gov/SECRS/2011/June/20110607/OP-1418/OP1418_053111_80002_310357154312_1.pdf (last visited Feb. 9th 2015, 4:19 PM) (Submission in response to Federal Reserve Request for information relating to Dodd-Frank Act section 216 Study regarding the resolution of financial companies under the bankruptcy code).

³⁵ *Id.* at 2–4.

³⁶ *Id.*

³⁷ *The Financial Institution Bankruptcy Act of 2014: Hearing Before Subcomm. on Regulatory Reform, Commercial and Antitrust Law of the Comm. on the Judiciary H.R.*, 113th Cong. 2nd Sess. 20–21 (2014) [hereinafter *FIBA Hearing*] (statement of Donald S. Bernstein, co-chair of the Insolvency and Restructuring Group at Davis Polk & Wardwell LLP).

proceedings can be slow and may allow failing institutions to linger in Chapter 11, rather than just being liquidated.³⁸ Opponents of the OLA argue that two potential options for dealing with resolution result in uncertainty and cause greater systemic risk.³⁹ What seems to be even more problematic is the huge amount of discretionary power given to the FDIC, which can essentially “pick winners and losers”⁴⁰ in deciding which firms would be liquidated.⁴¹ This type of vast discretion leaves certain creditors at the mercy of the FDIC and can lead to fundamental unfairness. Moreover, creditor uncertainty on how a SIFI would be resolved during a time of financial distress can lead to an overall decline in investing and would create more confusion, which would further result in some form of adverse systemic risk.⁴² Alternatively, bankruptcy has a proper foundation already in place, and with certain provisions added to the Bankruptcy Code, the problems caused by having multiple resolution mechanisms can be avoided. As stated by Congressman Bachus,⁴³ ranking member on the Financial Services Committee, “bankruptcy is open, transparent, and has clear rules, precedents, and a judge, which ensures fairness.”⁴⁴ Contrarily, OLA procedure would be carried out “behind closed doors”⁴⁵ and use government funds as regulators see fit, further supporting the notion that SIFI’s must be knowingly subjected to bankruptcy proceedings in the event of insolvency.⁴⁶

³⁸ Jamieson L. Hardee, *The Orderly Liquidation Authority: The Creditor’s Perspective*, 15 N.C. BANKING INST. 259, 263 (2011).

³⁹ *Id.*

⁴⁰ *Id.*; see also 156 CONG. REC. H5223, 5226 (daily ed. June 30, 2010) (Statement of Rep. Garret).

⁴¹ Hardee, *supra* note 38, at 263.

⁴² Hardee, *supra* note 38, at 264.

⁴³ Spencer Thomas Bachus III is a former U.S. Representative for the state of Alabama. He served from 1993–2015. He is a member of the Republican Party. As a member of the Republican Party, he served as chairman of the House Financial Services Committee (2011–2013).

⁴⁴ *Id.* (quoting 156 CONG. REC. H4289, 4289 (daily ed. June 9, 2010) (statement of Rep. Bachus).

⁴⁵ *Id.*

⁴⁶ *Id.*

Bankruptcy scholars such as Jeffery Lacker, argue that the bankruptcy process is preferable because "the alternatives are worse" and require the discretionary use of federal funds, which is an "unstable and unsustainable approach."⁴⁷ In response to a question about "too big to fail," Lacker said, "the combination of an enhanced Bankruptcy Code and the living will process will give regulators confidence that should a large financial institution experience distress, they will be able to resolve it through the bankruptcy process without extraordinary government assistance."⁴⁸

B. Title II and The Creation of The OLA Fail In Preventing Big Banks From Believing They Are "Too-Big-to-Fail."

A recent article in the Wall Street Journal quoted the FDIC's vice Chairman, Thomas Hoeing who stated, "my major worry is the perception that, since the passage of the Dodd-Frank Act, we have really become a much more sound and stable financial system, I question that."⁴⁹ Mr. Hoeing's concerns stem from the belief that big banks remain risky and they benefit from the perception that the U.S. would rescue them in a crisis.⁵⁰ Despite the fact that Dodd-Frank makes taxpayer bailouts illegal, the banks and policy makers choose not to believe what is on the paper.⁵¹ The reason is that the law allows for temporary government support and sends a message that banks will remain open for business in the face of insolvency, giving them an incentive to continue with risky business models.⁵² In order to relinquish this ideology, banks must be forced by regulators to put forth a proper "living will" that avoids taxpayer bailouts and has a

⁴⁷ See 2013 House Hearing, *supra* note 11 at 108 (statement of Jeffery Lacker in response to Rep. Jason Smith question asking Lacker to explain the benefits of resolving financial firms through the bankruptcy process).

⁴⁸ *Id.* ("Once this process becomes the norm, it will also shift incentives in financial markets and lead to less short-term funding, less maturity transformation, and less market fragility.").

⁴⁹ See Ryan Tracy, *The Man Who Has Wall Street Banks on Edge*, WALL ST. J., Sept. 26, 2014, at C1-C4.

⁵⁰ *Id.*

⁵¹ *Id.*

⁵² *Id.*

credible path in bankruptcy.⁵³ Therefore, in order to hinder financial firms from continuing the operation of risky business models and to prevent these firms from believing the Government will bail them out, distressed financial firms must be subjected to the bankruptcy process.

Moreover, if firms are subjected to a bankruptcy process, it becomes very important to properly equip the Bankruptcy Code with tools to necessary to facilitate the resolution of a failing financial firm. If the Bankruptcy Code is left in its current state, financial firms cannot adequately plan their “living will” and the possibility of the bailout may still seem viable in the eyes of a financial firm. If the “living wills” are deemed adequate by regulators, resolution of a firm should, in hindsight, be possible in bankruptcy, which supports the perception that financial institutions can no longer assume they will be put in receivership and bailed out by taxpayers.⁵⁴

Therefore, if these financial institutions know they will be subjected to bankruptcy and because of their “living wills” understand how they are going to liquidate or be reorganized, bankruptcy could theoretically damper a financial institution’s assumption that they will be rescued in the event of a financial crisis.⁵⁵

⁵³ *Id.*

⁵⁴ *Contra* Abby McCloskey & Paul H. Kupiec, *Why the ‘Living Will’ Process Sets Banks Up for Failure*, AM. BANKER (Aug. 11, 2014, (April 17, 2015, 4:22 PM), <http://www.americanbanker.com/bankthink/why-the-living-will-process-sets-banks-up-for-failure-1069285-1.html> (arguing that “living wills” allow regulators to restructure and change companies).

⁵⁵ The presumption of not being bailed out by the government also has to do with living wills being developed with the assumption of guaranteed financing in bankruptcy, through the form of Debtor in Possession funding. Many critics argue that this is unrealistic. See Gina Chon, *Fed Blow to Banks over ‘Living Wills,’* FIN. TIMES (Aug. 17, 2014, 4:22 PM), <http://www.ft.com/intl/cms/s/0/617d442c-24c4-11e4-ae78-00144feabdc0.html?siteedition=uk#axzz3NhofJlY8> (discussing that banks are precluded from assuming funding through the discount window during a time of financial stress).

More importantly, Title II's purpose to prevent taxpayer-funded bailouts of major financial institutions does not justify supplanting the Bankruptcy Code with the OLA.⁵⁶ Regulators point to the *ad hoc* bankruptcy of Lehman Brothers as the impetus for the enactment of the OLA pursuant to Title II. Regulators believe that if the Lehman Brothers estate had been placed in OLA receivership, it would have "imposed a lesser disruption on financial markets, and resulted in a greater recovery for Lehman's creditors, than . . . Lehman Brothers' filing under chapter 11."⁵⁷ Not only is this highly unlikely, but also the FDIC makes some peculiar criticisms to the Bankruptcy Code, stating that there are no parallel provisions in the Bankruptcy Code to effectively facilitate a transfer of a financial company's assets, liabilities, and operations to "one or more bridge financial companies for preservation of going concern, while less assets remain in receivership and are liquidated."⁵⁸ A Section 363 sale,⁵⁹ however, expressly authorizes the sale of property to an estate (analogous to a bridge company), and we can look to the automotive bankruptcy cases to see a very similar situation in the transfer of assets to a bridge company.⁶⁰ Further, if the goal of Title II is to liquidate failing companies, why is the FDIC contemplating restructuring? Is that not why we have the Bankruptcy Code? It seems that regulators, despite pronouncing bankruptcy as the resolution vehicle, are attempting yet another power-grab in an effort to remain relevant in the world of bank insolvency. In

⁵⁶ Sprayregen & Hessler, *supra* note 34, at 4.

⁵⁷ Sprayregen & Hessler *supra* note 34, at 4.

⁵⁸ Sprayregen & Hessler *supra* note 34, at 4.

⁵⁹ "Section 363 refers to the portion of the Bankruptcy Code that authorizes a debtor to sell its assets 'outside the ordinary course of business.'" Case S. Weil, *Section 363 of the Bankruptcy Code – A Tool for Buying and Selling Financially Distressed Assets*, (Sept. 3, 2013),

<http://www.lawmoss.com/content/uploads/2013/09/MBNews-2013-8-Section-363.pdf> Sales of assets "outside the ordinary course of business" are sales that are either unlike the sales that the debtor engages in his ordinary course of business. *Id.* "A Section 363 sale transfers the debtor's assets to a buyer in a discrete transaction that will be approved by the bankruptcy court if the debtor can demonstrate a "substantial business justification" for the sale." *Id.*

⁶⁰ See Stephanie Ben-Ishai & Stephen J. Lubben, *A Comparative Study of Bankruptcy As Bailout*, 6 BROOK. J. CORP. FIN. & COM. L. 79, 81 (2011).

addition, the FDIC points to the Bankruptcy Code's inability to guarantee access to debtor in possession ("DIP")⁶¹ financing, contrary to Title II where the FDIC is permitted to borrow funds from the Department of Treasury to make loans to, or guarantee, financial company obligations.⁶² The FDIC position is that if the Bankruptcy Code cannot quickly provide a funding source to a distressed SIFI, the delay in obtaining financing may destabilize the market. Additionally, DIP financing usually takes time to obtain and comes coupled with use restrictions from the lender. Typically these restrictions will devalue a financial firm and further limit their option in reorganizing or liquidation.⁶³ This Comment does take the stance that federal funding will likely be needed to facilitate the resolution of a SIFI, but it does not draw the conclusion that the OLA must be the resolution tool in order to provide this type of funding. If the goal of Title II is to "prevent bailouts, minimize moral hazard and market instability, . . . it is entirely counterintuitive not to require that DIP financing be subject to reasonable limitations such as market testing, creditor scrutiny, secured lender consent and conditions, the grant of additional security interest, and court approval."⁶⁴ The existence of providing federal funding in some form or another will continue to be an active debate, especially when contemplating

⁶¹ Upon a debtor filing a Chapter 11 bankruptcy petition the debtor is now called the "debtor in possession" and takes the role of a trustee in bankruptcy. Douglas J. Whaley & Jeffrey W. Morris, PROBLEMS AND MATERIALS ON DEBTOR AND CREDITOR LAW 391 (Vicki Been et al. eds., 5th ed. Wolters Kluwer Law & Business 2013); *see also* Marshall S. Huebner, *Debtor-In-Possession Financing*, THE RMA J., Apr. 2005, at 30, 31.

The DIP typically finds itself in need of credit immediately after initiating a Chapter 11 case. While most of its pre-bankruptcy liabilities are frozen, the company is likely to need cash immediately to cover payroll and the up-front costs of stabilizing the business. DIP loans are typically asset-based, revolving working-capital facilities put into place at the out-set of Chapter 11 to provide both immediate cash as well as ongoing working capital during the reorganization process. Perhaps most important, DIP financing helps the company restore vendor and customer confidence in the company's ability to maintain its liquidity. *Id.* when block-quoting, you don't need quotation marks

⁶² Sprayregen & Hessler, *supra* note 34, at 5–6.

⁶³ Sprayregen & Hessler, *supra* note 34, at 5–6; *see* FDIC QUARTERLY, THE ORDERLY LIQUIDATION OF LEHMAN BROTHERS HOLDINGS INC. UNDER THE DODD-FRANK ACT 31–49 (2011)

⁶⁴ Sprayregen & Hessler, *supra* note 34, at 6.

the “too-big-to-fail” phenomenon. But when taking a step back from the debate, this Comment argues that a revised Bankruptcy Code can facilitate the resolution of a SIFI without government funding but may be more effective if federal funding is in place as a last resort. Regardless, whether the funding is deemed necessary or not for resolution of a SIFI, the arguments above demonstrate the preference for bankruptcy and the unnecessary enactment of the OLA. As validated by the bankruptcy of Lehman Brothers, problems do exist with the ability of the bankruptcy process to handle resolution of a SIFI, which will be explored below. But by revising the Bankruptcy Code, the possibility of a government bailout is limited and financial firms that become distressed will have a properly formulated plan to be facilitated in bankruptcy.

III. THE PROBLEMS WITH THE CURRENT BANKRUPTCY CODE

“One of the most important questions facing policymakers today is whether the bankruptcy process is, or with modifications could be, a suitable method for handling the failure of complex financial firms.”⁶⁵ As suggested above, this Comment proposes that the Bankruptcy Code, as left by the Dodd-Frank Act to be the default mechanism, needs to be revised to accommodate these complex financial institutions and accomplish its presumptive goal of providing orderly resolution. This section of the Comment explores why the Bankruptcy Code needs to be revised in the light of its use during the 2008 bankruptcy of Lehman brothers. Lehman Brothers filed for Chapter 11 bankruptcy on September 15, 2008. Their filing became the largest and notably most complex filing in history, mainly because of its 209 subsidiaries in 21 different countries.⁶⁶ “The experience

⁶⁵ Thomas J. Fitzpatrick IV & James B. Thomson, *How Well Does Bankruptcy Work When Large Financial Firms Fail? Some Lessons from Lehman Brothers*, FED. RES. BANK OF CLEVELAND (Oct. 26, 2011), <http://www2.clevelandfed.org/research/commentary/2011/2011-23.cfm>.

⁶⁶ Joseph H. Sommer, *Why Bail-In? And How!*, 20 FED. RESERVE BANK OF N.Y., March, 2014 at 1–3.

of resolving Lehman Brothers in the bankruptcy courts has since led to an active debate regarding the effectiveness of U.S. Chapter 11 proceedings for complex financial institutions.”⁶⁷ Many critics of the bankruptcy process believe today’s distressed financial institutions would face the same problems as Lehman Brothers in bankruptcy, but are subsequently even more complex and involve multiple facets of business.⁶⁸ For example, the remaining large financial institutions involve investment banking, commercial banking, and insurance underwriting.⁶⁹ These financial institutions involved in the commercial banking world (which Lehman Brothers was not involved in) are capable of posing far greater risks to the financial system and to the economy, mainly because these brick-and-mortar establishments are integrated into the “real economy.”⁷⁰ Commentators argue that bankruptcy is ineffective for resolution of SIFIs for a number of reasons, starting with the length of the actual bankruptcy proceeding.⁷¹ It has been argued that the bankruptcy process takes too long and the lack of speed in bankruptcy prevents the preservation of value and the uncertainty about the potential duration of the automatic stay can further dissipate the value of assets.⁷²

A. *Qualified Financial Contracts Exemption to Automatic Stay*

The key feature to a bankruptcy proceeding is the automatic stay. This feature “prohibits creditors from taking steps to collect what they are owed once a debtor has filed

⁶⁷ *Id.*

⁶⁸ Stephen J. Lubben, *Resolution, Orderly and Otherwise: B Of A in OLA*, 81 U. CIN. L. REV. 485, 487–88 (2012).

⁶⁹ *Id.*

⁷⁰ *Id.*

⁷¹ *See generally id.*

⁷² BD. OF GOVERNORS OF THE FED. RESERVE SYS., *STUDY OF THE RESOLUTION OF FINANCIAL COMPANIES UNDER THE BANKRUPTCY CODE* (2011).

a bankruptcy petition.”⁷³ In effect, the stay halts the “race of diligence”⁷⁴ by creditors that might otherwise lead to haphazard liquidation of the firm’s assets, and instead allows for a more coordinated resolution of the firm’s financial distress.⁷⁵ Since the current Bankruptcy Code was enacted, Congress has gradually expanded exemptions for derivatives, repurchase agreements (“repos”)⁷⁶, and other “qualified financial”⁷⁷ contracts (QFCs).⁷⁸ Therefore, investors who are holding QFCs have the ability to immediately terminate and net-out their contracts or liquidate the collateral on their claims once a party has defaulted or filed for bankruptcy.⁷⁹ The problem is that these financial contracts are the primary assets of financial institutions, and the Bankruptcy Code’s safe harbor provisions permit a “run” on these assets.⁸⁰ To use Lehman Brothers as an example: when they filed for bankruptcy, QFC’s were exempted from the automatic stay, preference provisions, and the bankruptcy “anti-*ipso*” fact clause rules.⁸¹ This in turn caused the

⁷³ David A. Skeel, Jr. & Thomas H. Jackson, *Transaction Consistency and the New Finance in Bankruptcy*, 112 COLUM. L. REV. 152, 158 (2012).

⁷⁴ Race of diligence: this means that the first to perfect or to turn an inchoate into a choate lien wins. This generally must be done item by item because there is no general levy power. A secured creditor will win over an unsecured one. The first to record a judgment usually has the right to the good. Cite the source here as string.

⁷⁵ See Skeel, *supra* note 73, at 158.

⁷⁶ A repurchase agreement is a form of “short-term borrowing for dealers in government securities. The dealer sells the government securities to investors, usually on an overnight basis, and buys them back the following day.” INVESTOPEDIA, <http://www.investopedia.com/terms/r/repurchaseagreement.asp>

⁷⁷ See Pellerin & Walter, *infra* note 91, at 19 note. 27 (“In the Bankruptcy Code, contracts exempt from the automatic stay are referred to as ‘safe harbor contracts’ . . . The federal Depository institution act and the Dodd-Frank Act refer to the safe harbor contracts as QFCs. Since safe harbor contracts and QFCs generally refer to the same types of contracts, we will use the term QFC to refer to both, which is consistent with industry practice.”).

⁷⁸ Skeel, *supra* note 73, at 158.

⁷⁹ See Hardee, *supra* note 38, at 278.

⁸⁰ BD. OF GOVERNORS OF THE FED. RESERVE SYS., *supra* note 72, at 7.

⁸¹ “The phrase *ipso facto* is Latin for ‘by the fact itself.’ *Ipso facto* clauses are sometimes included in lease and purchase contracts, and they assert that if the lessee or purchaser becomes insolvent, or files for bankruptcy protection, then the contract has been breached. In other words, under such a clause the very act of filing for bankruptcy protection constitutes a breach of contract (hence the appellation, *ipso facto* clause) that absolves the other party of any further contract obligations.” Nicholas Gebelt, *Southern California Bankruptcy Law Blog*, available at <http://www.southerncaliforniabankruptcylawblog.com/2012/11/19/ipso-facto-clauses-in-bankruptcy/>.

‘spreads’ on credit default contracts (“CDS”)⁸² insuring Lehman Brothers’ debt to be seen as minimal instead of large (as default risks rise so does the spread).⁸³ Therefore, if the market recognized the CDS spread as large, market participants would have known Lehman Brothers was at the brink of insolvency. Because of the QFC’s exemption from the automatic stay, the market did not interpret Lehman Brothers as being at the threshold of default or insolvency until immediately before its collapse.⁸⁴ Additionally, the belief by CDS protection sellers that they would be bailed out if Lehman Brothers collapsed kept the price of CDSs low and therefore, the market saw Lehman Brothers as being in good financial health. Moreover, the special protections for derivatives added to this distortion and amplified the losses Lehman Brothers unexpected collapse caused in two ways.⁸⁵ First, bankruptcy’s special treatment of repurchase agreements invited a form of accounting manipulation used by Lehman Brothers at the end of each quarter to disguise

⁸² Stephano Giglio, *Credit Default Swap Spreads and Systemic Financial Risk*, Harvard University, Job Market Paper (Jan. 2011)

Credit default swaps are credit derivatives that allow the transfer of the credit risk of a firm between two agents for a predetermined amount of time. In a typical CDS contract, the protection seller offers the protection buyer insurance against the default of an underlying bond issued by a certain company (the reference entity). In the event of default by the reference entity, the seller commits to buy the bond for a price equal to its face value from the protection buyer. In exchange for the insurance, the buyer pays a quarterly premium, called the CDS spread, quoted as an annualized percentage of the notional value insured. If default occurs, the contract terminates, and the quarterly payments are interrupted. If default does not occur during the life of the contract, the contract terminates at its maturity date. A credit default swap is an insurance contract against the default of a firm, for example a financial institution. The ‘CDS’ spread corresponds to the yearly insurance premium.

⁸³ Vincent Ryan, *Do CDS Spreads Tell the Truth?*, CFO (Mar. 19, 2011), <http://ww2.cfo.com/banking-capital-markets/2011/05/do-cds-spreads-tell-the-truth-2/>.

⁸⁴ Stephen J. Lubben, *The Bankruptcy Code Without Safe Harbors*, 84 AM. BANKR. L.J. 123, 123–131 (2010) (noting that a credit default swap (CDS) provides the buyer with a payout if some underlying debt issued by the “referenced entity” defaults and that the value of the CDS is entirely dependent on the properties of the underlying reference obligations); see e.g., Stephen J. Lubben, *Credit Derivatives and the Future of Chapter 11*, 81 AM. BANKR. L.J. 405, 410–11 (2007); Anna Gelpern, *Domestic Bonds, Credit Derivatives, and the next Transformation of Sovereign Debt*, 83 CHI.-KENT L. REV. 147, 169 (2008)); see also Skeel, *supra* note 73, at 164–65; John B. Taylor, *DEFINING SYSTEMIC RISK OPERATIONALLY*, in *ENDING GOVERNMENT BAILOUTS AS WE KNOW THEM*, 46 (Kenneth E. Scott et al. eds., 2010) (arguing bankruptcy causes runs on repurchase agreements and fire sales of collateral underlying closed-out derivatives).

⁸⁵ *Id.*

the amount of its leverage. These transactions, now known as “105 transactions”⁸⁶ are ordinarily characterized as financing for accounting purposes. However, since these secured transactions are exempt from bankruptcy law, Lehman Brothers was able to characterize these repurchase agreement transactions as sales and shave millions in debt from their balance sheets. This recharacterization followed a delay in the recognition of Lehman Brothers’ true financial condition and as stated by David Skeel,⁸⁷ “almost certainly magnified the costs of its failure.”⁸⁸

The second contribution, by way of the derivatives exclusion to Lehman’s losses, can be seen by J.P. Morgan’s ability to seize and sell Lehman’s assets right before Lehman folded.⁸⁹ Lehman Brothers owed J.P. Morgan twenty billion dollars before they filed for bankruptcy and because derivative contracts are exempted from bankruptcy’s automatic stay provision, Lehman Brothers could not prevent J.P. Morgan from seizing and selling Lehman assets in lieu of the twenty billion.⁹⁰ Creditors who are able to rush in and seize assets are likely to grab assets, which are fundamental to the firm’s continued operations, so called “going-concern assets.”⁹¹ Going concern assets are important to a

⁸⁶ See generally Michael J. De La Merced & Julia Werdigier, *The Origins of Lehman’s ‘Repo 105,’* (March 12, 2010 7:02 a.m.) http://dealbook.nytimes.com/2010/03/12/the-british-origins-of-lehmans-accounting-gimmick/?_r=0 (“Repo 105 transactions were worth 105 percent of the cash it received”); See also INVESTOPEDIA, <http://www.investopedia.com/terms/r/repo-105.asp> (“An accounting trick in which a company classifies a short-term loan as a sale and subsequently uses the cash proceeds from said sale to reduce its liabilities. In the repo market, companies are able to gain access to the excess funds of other firms for short periods in exchange for collateral usually a bond”).

⁸⁷ David Skeel is the author of *The New Financial Deal: Understanding the Dodd-Frank Act and Its (Unintended) Consequences* (Wiley, 2011), as well as numerous articles and other publications. He has been interviewed on *The News Hour, Nightline, Chris Matthews’ Hardball (MSNBC), National Public Radio,* and *Marketplace*, among others, and has been quoted in the *New York Times, Wall Street Journal, Washington Post* and other newspapers and magazines.

⁸⁸ David A. Skeel, Jr. & Thomas H. Jackson, *Transaction Consistency and the New Finance in Bankruptcy*, 112 COLUM. L. REV. 152, 165 (2012).

⁸⁹ *Id.*

⁹⁰ *Id.*

⁹¹ See Sabrina R. Pellerin & John R. Walter, *Orderly Liquidation Authority as an Alternative to Bankruptcy*, 98 ECON. 1, 3–4 (2012); LAW LIB- AM. LAW AND LEGAL INFO, <http://law.jrank.org/pages/7169/Going->

firm that might be successfully reorganized. Such assets include operating equipment or property essential to the firm's operations. Furthermore, assets sold off separately are almost never worth more than if bundled together with other assets. This causes a reduction in the total amount creditors receive if the firm is liquidated and can prevent a firm from reorganization because of the asset seizures.⁹² Despite the possibility to receive more if assets are kept intact and bundled, creditors not subject to the automatic stay are individually incentivized to be the first to grab assets in an effort to recover a higher proportion of their debts than creditors who are slow to react. The counterargument to permitting the expansive protection for derivatives and repurchase agreements is to achieve the intended goal of "minimizing the systemic risks potentially arising from certain interrelated financial activities and markets."⁹³

Concern-Value.html (last visited Jan. 4, 2015); *see also* WEST'S ENCYCLOPEDIA OF AMERICAN LAW, <http://www.encyclopedia.com/doc/1G2-3437701998.html>.

Going Concern value is the value inherent in an active, established company as opposed to a firm that is not yet established. As a component of business value, going concern value recognizes the many advantages that an existing business has over a new business, such as avoidance of start-up costs and improved operating efficiency. In this sense, the going concern value of a firm represents the difference between the value of an established firm and the value of a start-up firm. Going concern value also indicates the value of a firm as an operating, active whole, rather than merely as distinct items of property. U.S. Bankruptcy law, for example, has recognized the need to preserve going concern value when reorganizing businesses in order to maximize recoveries by creditors and shareholders (11 U.S.C.A. § 1101 et seq.). Bankruptcy laws seek to preserve going concern value whenever possible by promoting the reorganization, as opposed to the liquidation, of businesses. WAS THE EMPHASIS ON "COMPONENT" IN THE ORIGINAL OR IS IT ADDED?

⁹²*Contra Pellerin & Walter, supra* note 91, at 3 (noting that QFCs can be immediately closed out because the collateral backing them will naturally not be complementary to other assets of the firm, nor will QFC collateral be vital to the firm's going-concern value. Such as exceedingly marketable or cash securities, which can be eliminated without undercutting the firm's ability to create loans or other financial products. Refuting this argument is that security backing some QFCs are firm specific and not all QFCs should be treated evenly).

⁹³ *See Sabrina supra* note 91, at 22 (citing Douglas H. Jones, Senior Deputy General Counsel, FDIC, Statement on Bankruptcy Reform Legislation, United States Senate (Mar. 25, 1999); *see also* Soo J. Yim & William J. Perlstein, "The Effect of Proposed Amendments to U.S. Insolvency and Banking Laws on Transactions Involving Securities, Commodities and Other Financial Contracts," 3 Prepared in connection with the American Bar Association 2001 spring meeting section of business law business bankruptcy committee forum on derivatives and proposed financial contract netting legislation (March 24, 2001) ("Immediate termination of outstanding contracts and liquidation of collateral facilities the acquisition of

Conversely, the idea of preventing systemic risk by allowing the safe harbor provision to apply to QFCs, did not prove accurate during the financial crisis. This is because, despite one form of systemic risk being reduced, the exemption promotes another form of systemic risk by allowing runs on repos⁹⁴ and fire sales⁹⁵ of the collateral underlying closed-out derivative contracts.⁹⁶ Again, in order to demonstrate the effects the exemption had on financial firms and the market, this Comment looks to the bankruptcy of Lehman Brothers. On the day of Lehman Brothers' bankruptcy filing, 733,000 of their 930,000 derivative counterparties sought to terminate their contracts.⁹⁷ This rush to close out positions and demand collateral added to the already-failing and weakened Lehman Brothers, while causing a negative effect on the financial market as parties rushed to sell their Lehman Brother shares and buy new positions with counterparties.⁹⁸ Bankruptcy scholar Stephen J. Lubben⁹⁹ argues that the 2005 Amendments to the Bankruptcy Code broadened the scope of "repurchase agreements" by including mortgage loans and interests in mortgage loans.¹⁰⁰ This in effect facilitated the already substantial use of short-term repo financing and contributed to the losses by encouraging excessive lending to mortgage originators.¹⁰¹ These arguments demonstrate

replacement contracts, reduces uncertainty and uncontrollable risk, improves liquidity and reduces the risk of rapid devaluation of collateral in volatile markets").

⁹⁴ See *Sabrina supra* note 91, at 23 n.39 (defining "runs on repos" as a situation where counterparties seize the collateral underlying these deposit-like instruments).

⁹⁵ See *Sabrina supra* note 91, at 23 n.40 (noting that the "phrase 'fire sale' typically refers to the possibility that the sale of an asset might yield a lower-than-typical price if holders of one type of asset attempt to sell en masse"). In comparison, the 'typical' (non-fire) price will result if sales are distributed over time. *Id.*

⁹⁶ See *Sabrina supra* note 91, at 23 (citing Edwards and Morrison 2005, Taylor 2010, Archarya et al. 2011).

⁹⁷ See *Sabrina supra* note 91, at 23.

⁹⁸ See Lubben, *supra* note 84, at 130–32.

⁹⁹ Stephen J. Lubben is the holder of the Harvey Washington Wiley Chair in Corporate Governance & Business Ethics at Seton Hall University School of Law and is an expert in the field of corporate finance and governance, corporate restructuring, financial distress, and debt. He is also the *In Debt* columnist for the *New York Times*' Dealbook page.

¹⁰⁰ See Lubben, *supra* note 84, at 130–32.

¹⁰¹ See Lubben, *supra* note 84, at 138–40.

that bankruptcy's special QFC treatment, as applied to SIFI's in financial distress, would not be ideal and a change is warranted in order to allow bankruptcy to be the proper mechanism for resolution.

B. Bankruptcy's Limited Sources of Funding.

Another problem with bankruptcy, as it currently exists, is its limited capability of providing adequate funding to a financial firm who is attempting to reorganize in Chapter 11. A firm attempting to reorganize in bankruptcy can obtain funds from a dismal array of sources, one consisting of the firm's very own assets or in the case of reorganization, potential debtor in possession ("DIP")¹⁰² financing.¹⁰³ Obtaining DIP financing is essential to the successful reorganization of a firm since it allows debtors to maintain sufficient liquidity to operate while reorganizing in Chapter 11. However, when faced with a financial crisis, funding must become available quickly in order to successfully reorganize.¹⁰⁴ This may be a difficult task for financial firms because of their inherent line of business. Assets of financial firms are usually highly obscure to outsiders and without careful analyses are very difficult to value.¹⁰⁵ As a result, DIP loans, which rely on the free market, may be very difficult to obtain in a time of financial distress.¹⁰⁶ "Section 364 of the Bankruptcy Code authorizes a post-petition creditor to receive priority in the distribution of the assets of the bankruptcy estate superior to all other creditors of the

¹⁰² For an explanation of debtor in possession financing *see supra* note 61..

¹⁰³ *See Pellerin & Walter, supra* note 91, at 13–14 (In reorganization, the distressed corporation, the debtor, continues to manage, or own, the troubled entity. Any loans to the distressed corporation are therefore loans to the DIP. *Id.* "Such loans are often senior to all former-prior to the bankruptcy filing-debts of the bankrupt firm. The prospect of being senior to other creditors allows funding to flow as long as creditors can be convinced that the firm is likely to survive and therefore repay"). *Id.*

¹⁰⁴ *Pellerin & Walter, supra* note 91, at 15.

¹⁰⁵ *Pellerin & Walter, supra* note 91, at 15.

¹⁰⁶ *See FIBA Hearing, supra* note 37, at 83–85 (statement of Stephen J. Lubben, Harvey Washington Wiley Chair in Corporate Governance & Business Ethics Seton Hall University School of Law).

estate... in order to make it possible to obtain funding.”¹⁰⁷ Regardless, if financial conditions do not allow the financial firm to obtain funding, there is no provision in the Bankruptcy Code authorizing the government to extend credit on this special preference basis; however, the U.S. and Canadian governments did fill the void when Chrysler and GM (collectively “GM”) were unable to obtain DIP financing.¹⁰⁸ The financial firm is then faced with the dilemma of liquidating or obtaining government monetary support. Some critics would say that any support from the government is a bailout and undermines the entire bankruptcy process, regardless of how and why regulators say it is not.¹⁰⁹ This Comment does not take a position as to whether any form of federal funding is a bailout, but it does take the position that some form of government funding as a backstop is necessary when facilitating the orderly resolution of a SIFI, even when deploying a bail-in strategy such as the SPOE, as discussed below.¹¹⁰ A major problem with bankruptcy is that, when dealing with a SIFI, it is simply unrealistic to count on free market DIP financing during a financial crisis. The use of Chapter 11 to reorganize GM demonstrates an effective way for the bankruptcy system to facilitate government funding to a financial firm without undermining the bankruptcy system itself. Conclusively, it is argued that the Bankruptcy Code should explicitly permit the government the capability of extending credit to a financial firm during times when DIP financing is unobtainable.¹¹¹

¹⁰⁷ BD. OF GOVERNORS OF THE FED. RESERVE SYS., *supra* note 72, at 13.

¹⁰⁸ Ben-Ishai & Lubben, *supra* note 60, at 80–81.

¹⁰⁹ Ben-Ishai & Lubben, *supra* note 60, at 80–81.

¹¹⁰ See discussion *infra* Part IV.

¹¹¹ See Pellerin & Walter, *supra* note 91, at 16 n.16 (“An alternative to bailouts or OLA that would address the problem of a lack of DIP funding as a result of SIFI opacity is to allow a troubled SIFI to enter reorganization, and permit the government to make DIP loans to the bankrupt firm. The government could quickly provide DIP funds to keep the firm from operating but the bankruptcy process could handle all other aspects of the resolution”); *Contra* Jeffrey M. Lacker, President, Federal Reserve Bank of Richmond, Speech at the Global Society of Fellows Conference at the University of Richmond: Ending ‘Too Big To Fail’ is Going to Be Hard Work (Apr. 9, 2013) (noting that a firm who properly manages liquidity in normal

But as the Bankruptcy Code stands, without revisions, the limited sources of funding available to a financial firm during reorganization lends to the belief that systemic effects may still occur. If a financial firm does not have access to secured liquidity after its recapitalization, it shortchanges the objectives and goals of recapitalization in the first place. Sure, bankruptcy would still be fine to let firms fail as Lehman Brothers did, but if the objective is to reorganize, some form of a lender of last resort need be in place.¹¹²

C. Bankruptcy's Domestic and Global Disruption

Financial institutions comparable in size to Lehman Brothers have an extensive domestic and global reach. Therefore, some of the most disastrous consequences of such an institutions failure occur outside the United States. In the case of Lehman Brothers, several Asian and London based subsidiaries failed, in part due to immediate loss of access to funds in Lehman Brothers management system.¹¹³ The worldwide effect of Lehman Brothers default confirmed the need for a resolution strategy that considered worldwide effects of financial institution distress.¹¹⁴ In spite of these worldwide systemic effects, Dodd-Frank did not address international consequences of a SIFI's collapse and neither the Bankruptcy Code nor the OLA are equipped to properly deal with worldwide systemic effects.¹¹⁵ Seemingly, regulators have suggested that SIFI's consider the effects their financial distress may have on foreign entities when putting forth their living will or resolution plan, but if these plans are tested against the Bankruptcy Code it becomes even

times prior to experiencing financial distress should be able line up funding without the support of government-provided DIP financing).

¹¹² See *FIBA Hearing*, *supra* note 37, at 33.

¹¹³ David A. Skeel, Jr., *Single Point of Entry and the Bankruptcy Alternative*, FACULTY SCHOLARSHIP PAPER 949, 6 (2014), http://scholarship.law.upenn.edu/faculty_scholarship/949.

¹¹⁴ *Id.*

¹¹⁵ *Id.* at 9.

more evident that the bankruptcy process must be able to resolve or hinder the worldwide effects of a distressed SIFI.¹¹⁶

As will be discussed below, if the SPOE approach works as intended, it will insulate foreign subsidiaries from a default by the parent company and limit the negative effects outside of the United States.¹¹⁷

D. Hybrid Approaches: The Call for Uniformity

A major concern when resolving SIFIs is the possible subjection to a barrage of insolvency regimes, both in the United States and in other countries.¹¹⁸ Undoubtedly, the involvement of multiple insolvency regimes complicated the bankruptcy of Lehman Brothers, and will continue to plague the resolution of SIFIs, if uncertainty exists on which resolution regime will be employed during a time of financial distress.¹¹⁹ Title I requires SIFIs to put forth a “living will” that will be tested under bankruptcy; a subsidiary, however, may be subject to another resolution regime.¹²⁰ As a result, resolution plans tend to adopt a hybrid approach in which some entities may be recapitalized or sold while others are wound-down.¹²¹ Advocates such as Donald Bernstein argue that “[t]he simplest way to avoid competing resolution proceedings would be to have a clear path to a single point of entry approach to financial firm insolvencies under the Bankruptcy Code.”¹²² This would avoid hybrid approaches, which cause higher implementation risk and the probability of larger losses for creditors and shareholders than

¹¹⁶ *Id.*

¹¹⁷ *See infra* pp. 25–26.

¹¹⁸ *See 2013 House Hearing, supra* note 11, at 84 (statement of Donald S. Bernstein).

¹¹⁹ *See 2013 House Hearing, supra* note 11, at 84 (statement of Donald S. Bernstein).

¹²⁰ Thomas H. Jackson, *Resolving Financial Institutions: A Proposed Bankruptcy Code Alternative*, BANKING PERSPECTIVE, Q. 1 2014, at 22, 24.

¹²¹ *See 2013 House Hearing, supra* note 11, at 84 (statement of Donald S. Bernstein).

¹²² *See 2013 House Hearing, supra* note 11, at 84 (statement of Donald S. Bernstein); *See* discussion on SPOE *infra* Part IV.

a pure SPOE approach.¹²³ Accordingly, as will be discussed *supra*, reforms that add tools to facilitate a SPOE approach to resolution in bankruptcy can eliminate many of these problems.

IV. THE FINANCIAL INSTITUTION BANKRUPTCY ACT OF 2014

FIBA 2014 is proposed legislation that amends the Bankruptcy Code by inserting tools which will allow it to facilitate a whole-firm recapitalization approach to resolving SIFIs. Particularly, the bill creates Subchapter V of Chapter 11, under which the assets of a financially troubled institution would be transferred to a bridge company, while its stock and long-term unsecured debt would be left behind in the old institution. The SIFI's property becomes the property of the newly-formed bridge company and ceases to be the property of the bankruptcy estate.¹²⁴ Supporters of the bill argue that whole-firm recapitalization (SPOE approach), as a means of resolving SIFI's, is by far the best approach without taxpayer-funded bailouts.¹²⁵ The SPOE approach to resolution is designed to avoid the abrupt unraveling of a financial firm and provide an efficient means to quickly disperse a distressed financial firm's losses on to shareholders and creditors so that "valuable components of the firm can continue business under new ownership and management, or be wound down in an orderly manner as going concerns."¹²⁶

Additionally, the primary purpose of the SPOE approach under FIBA 2014 "is to engender sufficient liquidity for the bridge financial company, to obtain private-sector financing by creating a 'clean' balance sheet through the transfer to it of assets stripped of

¹²³ See 2013 House Hearing, *supra* note 11, at 84 (statement of Donald S. Bernstein).

¹²⁴ Bruce Grohsgal, *Legislative Update, Why Recent SPOE For SIFI's Fail*, 33-12 ABIJ 10 (2014) (citing H.R. 5421, 113 Cong. (2014), § 1185(a)).

¹²⁵ FIBA Hearing, *supra* note 37, at 2-3 (statement of Donald S. Bernstein).

¹²⁶ FIBA Hearing, *supra* note 37, at 3 (statement of Donald S. Bernstein).

liabilities against which it can then borrow from the private sector.”¹²⁷ Therefore, the bill’s proposed amendments to the Bankruptcy Code allow for resolution of a SIFI in a manner that: 1) allocates losses among proper parties; 2) maximizes value for stakeholders; 3) minimizes systemic disruption and moral hazard; and yet 4) protects taxpayers from loss.¹²⁸ Most importantly, if bankruptcy is now capable of resolution, these enhanced bankruptcy procedures allegedly “create a level playing field between Wall Street and Main Street and ... assure [that] all parties know the rules of the game ahead of time.”¹²⁹ That said, Part IV of this Comment begins by describing the SPOE approach as implemented through bankruptcy and then analyzes its application to describe how it accomplishes the aforementioned goals.

A. *The Bail-in, Not Bail-out Strategy*

The single most important feature of the SPOE strategy is the source of the funding.¹³⁰ During the 2008 financial crisis, failing SIFI’s were rescued by funds outside the institution in the “form of taxpayer assistance via a direct intervention by the sovereign government,” hence a bailout.¹³¹ Conversely, the SPOE approach allows for funds to come from within the institution, particularly in the form of subordinate debt, henceforth a bail-in.¹³² The SPOE strategy is made possible by the structure of large U.S. financial institutions. These institutions have a “top-level holding company whose capital structure includes substantial amounts of bonds and other long-term unsecured debt but relatively

¹²⁷ Grohsgal, *supra* note 124.

¹²⁸ Letter from National Bankruptcy Conference, to Senators Cornyn and Toomey regarding R. 1861–Taxpayer Protection and Responsible Resolution Act (Jan. 29, 2014).

¹²⁹ See Hardee, *supra* note 38, at 263; See 156 Cong. Rec. H5223, 5226 (daily ed. June 30, 2010) (statement of Rep. Capito).

¹³⁰ Jim Fuchs, *From Bailouts to Bail-ins: Will the Single Point of Entry Concept End “Too-Big-To-Fail”?*, CENTRAL BANKER, Summer 2013, at 5–6.

¹³¹ *Id.*

¹³² *Id.*

few derivatives and other short term debt.”¹³³ With less short-term debt and derivative contracts, holding companies are much less susceptible to a run on their assets. This is because assets at the holding company level, such as bonds, even if sold by their holders, do not extract liquidity from the financial institution, making the holding company structure a great candidate for the SPOE approach.¹³⁴ The holding company structure was established by large US financial institutions because of restrictions put on a bank’s ability to branch across state lines and hurdle other preventative regulations in the banking industry. It is merely a pleasant surprise that these financial structures designed to avoid regulation, allow for the implementation of the SPOE strategy.¹³⁵ With the holding company structure in place, resolution involves proceedings only at the parent holding company level and allows all operating subsidiaries to remain open for business.¹³⁶ The operating subsidiaries would then be recapitalized with assets from the holding company and would continue operation as part of a newly created debt-free bridge holding company.¹³⁷ Furthermore, by only placing the old holding company into resolution proceedings and not its subsidiaries, systemic effects are limited because critical subsidiaries are kept out of resolution and are provided with liquidity from the new holding company.¹³⁸ More importantly, with the establishment of a new bridge company, the old holding companies creditors and shareholders are left behind to bear the losses in

¹³³ See Skeel, *supra* note 113, at 9.

¹³⁴ Lubben, Stephen J., *OLA after Single Point of Entry: Has Anything Changed?* (November 11, 2013). Seton Hall Public Law Research Paper (No. 2353035) at 2, available at SSRN: <http://ssrn.com/abstract=2353035> or <http://dx.doi.org/10.2139/ssrn.2353035>.

¹³⁵ See Skeel, *supra* note 113, at 2.

¹³⁶ See *FIBA Hearing*, *supra* note 37, at 16 (statement of Donald S. Bernstein); FDIC ADVISORY COMM. ON SYSTEMIC RESOLUTION, *The Single Point of Entry Resolution Strategy* (Dec. 11, 2013), available at https://www.fdic.gov/about/srac/2013/2013_12_11_presentation_title-ii.pdf.

¹³⁷ *FIBA Hearing*, *supra* note 37, at 16 (statement of Donald S. Bernstein).

¹³⁸ *FIBA Hearing*, *supra* note 37, at 17 (statement of Donald S. Bernstein).

bankruptcy.¹³⁹ Under the new SPOE approach, bankruptcy now has the tools to: “(1) create and transfer the failed holding company’s assets to a bridge financial company; (2) impose a temporary stay on financial contract terminations and a temporary override or cross-defaults; (3) the ability to assume financial contracts and related guarantees; and (4) the availability of temporary secured liquidity.”¹⁴⁰ Is there now a workable alternative to the OLA and does Subchapter V provide superior protection against another financial crisis; have we ended “too-big-to-fail”? These questions are not yet answered and it remains unlikely they become answered until the SPOE strategy is tested in the marketplace. Conversely, what is answered by amending the Bankruptcy Code is that there now exists a workable alternative to the OLA and the Bankruptcy Code is capable of providing resolution to troubled financial firms or SIFI’s. The following subparts will explore how resolution proceedings are commenced and undergone via the new Subchapter V.

1. Tri-party balancing act, consideration of debtors, creditors and governmental aims when commencing Subchapter V proceedings.

Under Subchapter V, proceedings with respect to a “covered financial institution”¹⁴¹ can commence either voluntarily by the distressed firm or involuntarily by the Federal Reserve Board (“FRB”).¹⁴² Subchapter V takes a middle ground position by

¹³⁹ *FIBA Hearing, supra* note 37, at 17 (statement of Donald S. Bernstein).

¹⁴⁰ *FIBA Hearing, supra* note 37, at 16 n. 2 (statement of Donald S. Bernstein).

¹⁴¹ “The Dodd-Frank Rule applies to ‘covered companies,’ which is defined to include (i) any U.S. bank holding company that has \$50 billion or more in consolidated assets, (ii) any foreign bank or company that is a bank holding company, or that is treated as a bank holding company, with \$50 billion or more in total consolidated assets, and (iii) any nonbank financial company supervised by the Board Implementing Section 165(d) of the Act)” Memorandum from Skadden, Arps, Slate, Meagher & Flom LLP & Affiliates on the Dodd-Frank requirement for covered financial institutions to develop global contingency plans (Sept. 23, 2011).

¹⁴² *See FIBA Hearing, supra* note 37, at 22 (statement of Donald S. Bernstein).

adopting a two-scenario approach to commencing proceedings.¹⁴³ Subchapter V ultimately does not give all the power to the FRB nor leaves it solely in the hands of the financial firm when contemplating relief in bankruptcy. In a conventional bankruptcy case, only the debtor (voluntarily) or its creditors (involuntary) are able to commence proceedings for the purpose of enforcing their own respective rights and obligations.¹⁴⁴ Contrarily, under Title II, proceedings to be put into OLA receivership are involuntarily initiated by the federal government for the main purposes of preventing a financial crisis and another taxpayer bailout, as in 2008.¹⁴⁵ Subchapter V, as stated above, may commence by the debtor or the FRB for purposes of reorganizing the failing firm and preventing harm to market stability.¹⁴⁶ Therefore, this approach increases the likelihood that the aim of creditors (maximizing their return), debtors (reorganizing the distressed firm), and the government (preventing market contagion) are achieved when commencing proceedings.¹⁴⁷ Decisively, this minor but important revision to commencing proceedings encourages financial corporations to pursue restructuring options and limits the government's discretionary power to involuntarily invoke proceedings¹⁴⁸ by subjecting them to the Bankruptcy Court for determination that their decision "shown by a preponderance of the evidence is necessary to prevent imminent substantial harm to

¹⁴³ See *FIBA Hearing*, *supra* note 37, at 66 (statement of Steven E. Hessler).

¹⁴⁴ See *FIBA Hearing*, *supra* note 37, at 66 (statement of Steven E. Hessler).

¹⁴⁵ *FIBA Hearing*, *supra* note 37, at 66 (statement of Steven E. Hessler).

¹⁴⁶ *FIBA Hearing*, *supra* note 37, at 66 (statement of Steven E. Hessler).

¹⁴⁷ *FIBA Hearing*, *supra* note 37, at 66 (statement of Steven E. Hessler).

¹⁴⁸ *FIBA Hearing*, *supra* note 37, at 76 (statement of Steven E. Hessler) (citing 11 U.S.C. §§ 1107, 1108 (2012)) ("Chapter 11 applies the concept of a "debtor in possession retaining the ability to manage its business post-petition...this ensures that decision makers of distressed corporations are not disincentivized from pursuing the difficult but necessary restructuring decisions that may involve or lead to a Chapter 11 filing").

financial stability in the United States.”¹⁴⁹ The next subpart will address the proposed treatment of QFC’s under Subchapter V.

B. The Automatic Stay as Applied to Qualified Financial Contract s

As previously stated, the treatment of qualified financial contracts in bankruptcy and its application to Lehman Brothers caused chaos and major disruption in the market place.¹⁵⁰ Consequently, Subchapter V helps to limit some of that disruption by subjecting QFC’s to the automatic stay, even if for only forty-eight hours. First, in order to facilitate the transfer of any derivatives and short-term debt to the newly created bridge entity, §1188 of the bill permits a stay of forty-eight hours from the commencement of proceedings on qualified financial contracts.¹⁵¹ The stay halts a ‘run’ by the institutions derivative counterparties long enough to facilitate the transfer to the newly created bridge holding company.¹⁵² Furthermore, the stay is essential to successfully make the transfer of assets to the bridge company. This is because without the stay there would unlikely be any assets left by creditors to transfer to the bridge company. Additionally, the proposed legislation addresses the issue of QFC location. Most of financial firms QFC’s are in the operating subsidiaries of the holding company. Consequently, one of the most important provisions of the bill is bankruptcy’s ability to override cross-defaults in QFC’s pursuant to §1188(f). Cross-default provisions are contracts that have been entered into by the debtor’s affiliates or subsidiaries that “make the debtor’s bankruptcy a default under the affiliate contract,” hence the ability of the counterparty to now terminate the contract, in which they are then capable of making a run at the firms going concern assets essential to

¹⁴⁹ See *FIBA Hearing*, *supra* note 37, at 70 (statement of Steven E. Hessler)(citing § 1183(a)(2)(A)(iv)).

¹⁵⁰ See Skeel, *supra* note 113, at 14-18.

¹⁵¹ Financial Institution Bankruptcy Act of 2014, H.R. 5421,113th Cong. §1188 (2014); Skeel, *supra* 113, at 16.

¹⁵² *FIBA Hearing*, *supra* note 37, at 28 (statement of Donald S. Bernstein).

the operation of vital subsidiaries.¹⁵³ Section 1188(f) limits these counterparty termination rights crucial to the SPOE recapitalization.¹⁵⁴ As stated by Donald Bernstein before the Subcommittee on Regulatory Reform, Commercial, and Antitrust Law:

“Overriding cross-defaults in QFCs of affiliates of a covered financial corporation is crucial to a single point of entry recapitalization because affiliate QFCs are often guaranteed by the holding company and, if the holding company files for bankruptcy or loses its credit rating, termination rights may be triggered, even though the affiliate counterparty is healthy, well capitalized (having been recapitalized) and has not been placed into bankruptcy proceedings or receivership. These cross-defaults to the holding company’s bankruptcy or downgrades accordingly need to be overridden by the statute if the external counterparty’s termination rights are to be eliminated.¹⁵⁵”

Therefore, enabling the automatic stay to incorporate QFC’s and override the safe harbor provisions, bankruptcy is able to limit some of the systemic effects caused by a run on assets, provide liquidity to the new bridge company, and preserve a distressed financial firms books.

C. International Standard for the Resolution of Global SIFI’s

The United States and the United Kingdom have heavily interconnected markets, and the U.K. possesses the highest counterparty credit exposure of the largest U.S. financial firms.¹⁵⁶ Therefore, through a cooperative SPOE or bail-in strategy for both party’s systemic banks, resolution proceedings for host country operations are unnecessary.¹⁵⁷ The key to both the U.S. and the U.K. believing in the SPOE strategy as their preference “is the fact that recapitalization and bail-in strategies allow the firms to continue their business and meet their operating

¹⁵³ Skeel, *supra* note 113, at 15.

¹⁵⁴ *FIBA Hearing, supra* note 37, at 29 (statement of Donald S. Bernstein).

¹⁵⁵ *FIBA Hearing, supra* note 37, at 29 (statement of Donald S. Bernstein).

¹⁵⁶ *See*, Memorandum from International Monetary Fund on Cross-Border Bank Resolution, prepared by IMF staff to brief the Executive Board on June 9, 2014 (June 2, 2014).

¹⁵⁷ *FIBA Hearing, supra* note 37, at 19 (statement of Donald S. Bernstein).

obligations in the ordinary course in both home and host countries. As a result, local regulators should not feel compelled to take precipitous actions that can hinder the resolution of the overall group.”¹⁵⁸ Irrefutably, because Subchapter V of the Financial Institution Bankruptcy Act of 2014 employs a SPOE strategy, the bill brings us closer to solving global disruption of failing systemically important financial institutions.

V. THE REMAINING PROBLEMS WITH THE BANKRUPTCY CODE

Resolution of a SIFI should be done in a manner that maximizes value for stakeholders, minimizes systemic disruption and moral hazard, and protects taxpayers from loss.¹⁵⁹ The proposal of a bail-in strategy through the addition of a Subchapter V to the Bankruptcy Code does further these aims. Unfortunately, issues still exist that need to be addressed if the Bankruptcy Code is going to successfully create a uniform regime to resolve distressed financial firms.

A. *The Liquidity Shortfall*

The most glaring concern when implementing the SPOE approach through the Bankruptcy Code is its failure to address the problem of obtaining “new” capital for liquidity purposes.¹⁶⁰ Access to liquidity is essential because without it, “regulators and the market will lack the confidence needed to preserve at least a minimal sense of calm without which all parties—regulators, counterparties and other market participants- will race to seize assets and withdraw liquidity at all levels of the SIFI.”¹⁶¹ Therefore, in order to accomplish a stabilization of the marketplace and the restructuring of a financial

¹⁵⁸ *FIBA Hearing, supra* note 37, at 20 (statement of Donald S. Bernstein).

¹⁵⁹ *2014 Hearing, supra* note 25, at 56 (statement of Jane Lee Vris).

¹⁶⁰ *See 2014 Hearing, supra* note 25, at 57 (statement of Jane Lee Vris, chair of Capital Markets Committee, National Bankruptcy Conference, Partner and General Counsel, Millstein & Co., L.P.).

¹⁶¹ *See 2014 Hearing, supra* note 25, at 57 (statement of Jane Lee Vris).

institution, immediate liquidity is needed. New liquidity does not consist of the transferred assets to the bridge company as explained earlier, but must be obtained from another source, such as in the form of DIP loans. The problem rests with obtaining DIP funding during a time of financial distress; this may be difficult and time consuming, which is not ideal for the resolution of a SIFI. Even under the best of circumstances, the market will need to divulge the information about the restructuring of the financial firm before market participants will begin to extend credit. More broadly, any delay in time waiting for market liquidity to return can be detrimental to the successful restructuring of the financial institution. As argued by bankruptcy scholar Stephen J. Lubben:

Successful recapitalization is going to depend on the value of the enterprise. That value will be largely a function of the value of the SIFI's subsidiaries, perhaps with a little premium that reflects the synergies of having all those subsidiaries working together under a single roof. If that value is no longer sufficient to support the capital the financial institution needs, there remains a major problem. Either losses will have to be imposed at the subsidiary level to cut down the size or the FDIC will simply have to inject value into the institution.¹⁶²

If the FDIC does provide liquidity to the institution we are left with the question of “is this another bailout?” In short, if the FDIC uses taxpayer funds to prevent the liquidation of a financial company, many opponents of reforming the Code will be in uproar. The truth is that some mechanism must be in place to provide for an additional source of backstop liquidity to prevent flight of short-term capital and stabilize the institution, particularly if there is a risk of contagion.¹⁶³ After a financial firm is recapitalized through the SPOE approach it defeats the entire purpose to not provide sufficient liquidity in the event the firm needs it to fend off a liquidity run.¹⁶⁴ This is extremely important especially when it

¹⁶² See Lubben, *supra* note 134, at 3.

¹⁶³ See *FIBA Hearing*, *supra* note 37, at 33. (statement of Donald S. Bernstein).

¹⁶⁴ See *FIBA Hearing*, *supra* note 37, at 33. (statement of Donald S. Bernstein).

comes to SIFIs. Distressed banks have had access to funding through the discount window during times of financial distress in order to prevent or fund a run on their assets and diversified financial institutions with broker dealers, insurers, and other operating subsidiaries must have access to credit support other than through the public markets to do the same.

Donald Bernstein, co-chair of the Insolvency and Restructuring Group at Davis Polk & Wardwell LLP says, “after three-and-a-half decades of experience working with troubled companies, that the simple availability of a committed liquidity source is the best way to assure that the liquidity source is not needed.”¹⁶⁵ Furthermore, to subvert the too-big-to-fail and bail-out arguments, the liquidity provided would not be risk capital.¹⁶⁶ It would be provided to healthy firms on a secured basis in order to protect taxpayers from loss.¹⁶⁷ With the development of the SPOE mechanism and the safeguards put in place to protect taxpayers, now, in this post financial crisis world is the time for bankruptcy law to reconcile illiquidity problems caused by creditor-runs.¹⁶⁸ If bankruptcy law can sufficiently address this glaring problem posed by distress SIFI’s, bankruptcy can effectively end too-big-to-fail and simultaneously prevent the market turmoil caused in the 2008 crisis.

VII. CONCLUSION

As evidenced by the proposed amendments to the Bankruptcy Code, the resolution of a SIFI is now possible to facilitate by the Bankruptcy Code. Furthermore, by

¹⁶⁵ See *FIBA Hearing*, *supra* note 37, at 33. (statement of Donald S. Bernstein).

¹⁶⁶ See *FIBA Hearing*, *supra* note 37, at 33. (statement of Donald S. Bernstein).

¹⁶⁷ See *FIBA Hearing*, *supra* note 37, at 33. (statement of Donald S. Bernstein).

¹⁶⁸ David A. Skeel & Kenneth Ayotte, *Bankruptcy Law as a Liquidity Provider*, 80 U. CHI. L. REV. 1557, 1622-24 (2013) (arguing that “many of bankruptcy’s existing rules, including debtor-in-possession financing, sales free and clear of liens, and coerced loans, can be seen as liquidity-providing rules that target either debt-overhang problems, adverse-selection problems, or both”).

implementing the SPOE mechanism into bankruptcy, the courts now have a sensible tool they can use to resolve a SIFI, while preserving due process.¹⁶⁹ The SPOE approach coupled with bankruptcy is one of the most important innovations to emerge after the implementation of Dodd-Frank Act. Nevertheless, SPOE as implanted in bankruptcy, still possess some concerns about speed and access to liquidity.¹⁷⁰ Based on the remaining problems, it is likely that the government must still act as a lender of last resort, and it remains to be seen whether the market conditions during a crisis allow for an SPOE approach to work smoothly. Therefore, the elimination of the too-big-fail phenomenon is unlikely, but it does take a step in the right direction solving the major issues surrounding the 2008 financial crisis.

¹⁶⁹ *Supra* note 113, at 18.

¹⁷⁰ *FIBA Hearing supra* note 37, at 34.

