1991

The Implied Good Faith Filing Requirement: Sentinel of an Evolving Bankruptcy Policy

F. Stephen Knippenberg, *University of Oklahoma College of Law*
Lawrence Ponoroff

Northwestern University Law Review

Printed in U.S.A.
Vol. 85, No. 4

LEGAL THEORY

THE IMPLIED GOOD FAITH FILING REQUIREMENT: SENTINEL OF AN EVOLVING BANKRUPTCY POLICY

*Lawrence Ponoroff**
*and F. Stephen Knippenberg***

INTRODUCTION

For most of this century, bankruptcy operated in the backwater of legal practice and commentary. Coincident with the modernization of federal bankruptcy law accomplished under the Bankruptcy Reform Act of 1978,[1] however, the reclusive world of bankruptcy began to change rapidly. The past decade has occasioned an unprecedented profusion of bankruptcy filings and a concomitant explosion in the volume of reported bankruptcy decisions.[2] Commercial debtors have shown an increased willingness to use the bankruptcy law both as a tactic in business litigation and as an instrument of business planning.[3] Of equal importance,

* Professor of Law and Associate Dean for Academic Affairs, University of Toledo College of Law. J.D., 1978, Stanford University; A.B., 1975, Loyola University of Chicago.

** Associate Professor of Law, University of Oklahoma Law Center. L.L.M., 1987, Temple University; J.D., 1980, University of Tulsa; B.A., 1974, University of Dayton.

The authors wish to thank William J. Woodward and David Gray Carlson, each of whom offered thoughtful suggestions based on a reading of an earlier draft of this Article.

1 Pub. L. No. 95-598, 92 Stat. 2549 (1978) (effective Oct. 1, 1979) [hereinafter the Reform Act]. Title I of the Reform Act was codified as 11 U.S.C. §§ 101-700. Unless otherwise indicated, references in this Article to the "Bankruptcy Code" or the "Code" are to Title 11 of the United States Code as amended through January 3, 1989, 11 U.S.C. §§ 101-1330 (1988).

2 According to statistics compiled and maintained by The Administrative Office of the United States Courts, the total number of bankruptcy filings increased from 226,476 for the fiscal year ended June 30, 1979 (the last full year governed by the Bankruptcy Act of 1898, ch. 541, 30 Stat. 544 (the Nelson Act)) to 594,567 for the fiscal year ended June 30, 1988. *See* U.S. CTS. DIRECTOR OF ADMIN. ANN. REP. 1979, at 573; *id.* 1988, at 360. For calendar year 1989, total filings had increased to 679,980. ADMIN. OFF. U.S. CTS., TABLES OF BANKR. STATISTICS DURING THE TWELVE MONTH PERIOD ENDED DEC. 31, 1989 (Table F2A) [hereinafter 1989 TABLES]. Over approximately the same period of time, it took over 100 volumes of West's *Bankruptcy Reporter* to house all the reported bankruptcy decisions of United States courts. *See also infra* note 82.

3 While still a small percentage of aggregate bankruptcy filings, the number of business bankruptcy reorganizations has more than doubled since 1980 from 7,230 for the fiscal year ended June 30, 1981 to 16,620 for the fiscal year ended June 30, 1988. U.S. CTS. DIRECTOR OF ADMIN. ANN. REP. 1981, at 552; *id.* 1988, at 364. For calendar year 1989, business bankruptcy reorganizations totaled 17,798. 1989 TABLES, *supra* note 2.

bankruptcy has become big business,[4] as evidenced by the relatively recent phenomenon of filings by major business enterprises whose principal motivation for seeking bankruptcy court protection has been related in only the most attenuated sense to the immediate financial distress customarily associated with bankruptcy proceedings.

The circumstances and motivations that have driven solvent corporations with positive and consistent cash flow to attempt reorganization under the Bankruptcy Code have been varied. These filings, however, all have something in common—they represent an attempt by managers of corporate debtors to solve a particular problem or respond to a particular business exigency which, for whatever reasons, cannot be satisfactorily addressed by resort to traditional legal institutions or the political process. Necessarily, the increase in commercial bankruptcy filings means that the impact of the federal bankruptcy law is now being felt by a much broader spectrum of societal interests. It also means that bankruptcy law is evolving in new and, as yet, unexplored directions. These developments, in turn, are triggering greater recognition from both political and academic quarters of bankruptcy law as a potential tool for effecting major social and economic policy.

The expanded uses of the bankruptcy law by companies that a decade earlier would never have seriously entertained the idea of initiating a bankruptcy proceeding could not have been foreseen at the time the Bankruptcy Code was enacted. Accordingly, Congress has addressed the issues raised by unconventional filings in an essentially ex post, piecemeal, and ad hoc fashion.[5] The process has been far from ideal. The

---

4 For example, the *New York Times* reported that total professional fee applications in Texaco Inc.'s Chapter 11 case (which, by customary standards, was a remarkably abbreviated one) exceeded $50 million. N.Y. Times, July 8, 1988, at B20, col. 1. Similarly, the amount of initial fee applications in the Eastern Airlines, Inc. bankruptcy has been reported at $7.4 million. Blum, *Eastern Fee Requests*, Nat'l L.J., Aug. 28, 1989, at 2, col. 1.

5 The Continental Airlines reorganization drew critical attention to the use of bankruptcy as a tool for avoiding collectively bargained labor agreements. *See In re* Continental Airlines Corp., 38 Bankr. 67 (Bankr. S.D. Tex. 1984), discussed *infra* text accompanying notes 45-48. Later that same year, the Supreme Court decided NLRB v. Bildisco & Bildisco, 465 U.S. 513 (1984). In that far-reaching decision, the Court, by a five-to-four margin, upheld both the debtor-in-possession's right to reject a collective bargaining agreement upon a showing that the agreement burdens the estate, and the right of the debtor-in-possession to unilaterally modify or treat its collective bargaining agreements as rejected until formal rejection is approved or denied by the bankruptcy court. *Id.* at 526. Largely in response to organized labor's unhappiness with *Bildisco*, Congress added § 1113 to the Bankruptcy Code as part of the Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, § 541(a), 98 Stat. 333, 390 (1984). That section sets forth more detailed standards for rejection of collective bargaining agreements and overrules *Bildisco* by compelling the debtor-in-possession to negotiate modifications of its labor contract in good faith before petitioning the court for rejection. *See generally* White, *The Bildisco Case and the Congressional Response*, 30 WAYNE L. REV. 1169 (1984).

Another major Chapter 11 filing, LTV Steel Co. v. David Graham Co. (*In re* Chateaugay Corp.), 78 Bankr. 713 (Bankr. S.D.N.Y. 1987), caused Congress to tinker with the Bankruptcy Code again, this time to protect the interests of former, rather than current, employees of a Chapter 11 post-1978 amendments to the Bankruptcy Code have been reactive in nature, the product of a mind-set bent on "righting past wrongs." In part, this may be attributable to the sense of urgency and the inevitable horse-trading that characterize a highly political arena. However, the muddled nature of the process also may be due to the absence, until recently, of any rigorous or systematic analysis of the theory of bankruptcy.[6]

Tactical use of the bankruptcy system—whether to avoid specific labor or environmental obligations, circumvent state law requirements governing appeal bonds, or effectively consolidate and remove to a federal tribunal the resolution of multiple products liability claims—has also caused the judicial branch to rethink the question of what standards and criteria should regulate entitlement to bankruptcy relief. Armed initially with only sparse eligibility standards contained in the Code,[7] bankruptcy

---

debtor. The debtor in *Chateaugay* had suspended all post-petition payments of retirees' (as contrasted with current employees') benefits pending further orders of the court, based on its interpretation that 11 U.S.C. § 1113 did not mandate such payments. Congress responded by amending the Bankruptcy Code to avoid recurrence of this situation in the future. *See* Retiree Benefits Bankruptcy Protection Act of 1988, § 2, 11 U.S.C. § 1114 (1988).

In 1988, Congress also added a new subsection (n) to 11 U.S.C. § 365 in order to overrule the perceived impact of the Fourth Circuit's decision in Lubrizol Enterprises. v. Richmond Metal Finishers, 756 F.2d 1043 (4th Cir. 1985), *cert. denied*, 475 U.S. 1057 (1986). In that case, the court held that rejection of a technology license agreement deprived the licensee of any right to continue to use the technology even though the agreement provided for continued use upon the debtor's breach. *Id.* at 1048. Deciding that Lubrizol unreasonably restricted the licensing of technology and other intellectual property, Congress enacted the Intellectual Property Licenses in Bankruptcy Act of 1988 to secure and protect the rights and interests of intellectual property licensors and licensees. Pub. L. No. 100-506, 102 Stat. 2538 (1988). See S. REP. No. 505, 100th Cong., 2d Sess. 1, *reprinted in* 1988 U.S. CODE CONG. & ADMIN. NEWS 3200, 3200-04, for an explanation of the reasoning leading to the adoption of the legislation and its operation in protecting intellectual property licensees in subsequent cases.

6 Over the past several years, Dean Jackson and others have brought economic analysis to bear in developing a theoretical model to explain the existence and limits of positive bankruptcy law rules. *See generally* Baird & Jackson, *Corporate Reorganizations and the Treatment of Diverse Ownership Interests: A Comment on Adequate Protection of Secured Creditors in Bankruptcy*, 51 U. CHI. L. REV. 97 (1984); Jackson, *Bankruptcy, Non-Bankruptcy Entitlements, and the Creditors' Bargain*, 91 YALE L.J. 857 (1982); Jackson & Scott, *On the Nature of Bankruptcy: An Essay on Bankruptcy Sharing and the Creditors' Bargain*, 75 VA. L. REV. 155 (1989). The impact of this analysis on the question of a good faith filing prerequisite is discussed *infra* text accompanying notes 118-119. *See also infra* note 82 and accompanying text.

7 The Bankruptcy Code's eligibility standards for voluntary bankruptcy relief are contained in 11 U.S.C. § 109 (1988). Generally, any individual or non-government entity (exclusive of stockbrokers, commodity brokers, banking institutions, and insurance companies) with a residence, domicile, place of business, or property located in the United States may seek relief under Chapter 11. 11 U.S.C. § 109(a), (b), (d) (1988).

Conspicuous by its absence from the Bankruptcy Code is any requirement that the debtor be insolvent in either an equity or balance sheet sense. This is in marked contrast to the requirements for commencement of both voluntary and involuntary proceedings under the prior Bankruptcy Act. Under that law, the petitioner in either a voluntary or involuntary Chapter X (corporate reorganization) proceeding had to allege and be prepared to prove that the debtor was balance sheet insolvent courts have responded to the unanticipated surge in "creative"[8] Chapter 11 filings by fashioning an entry barrier of their own.[9] Specifically, a growing number of courts have entertained preliminary motions to dismiss reorganization proceedings based upon the breach of an implied requirement that the petition be filed in "good faith."[10]

or unable to pay its debts as they matured. Chandler Act, ch. 575, § 130, 52 Stat. 840, 886 (1938) (codified as 11 U.S.C. § 530 and repealed in 1978). Similarly, a voluntary Chapter XI arrangement of unsecured debt (the sole type allowed) could only be brought if the debtor was "insolvent or unable to pay his debts as they mature[d]." *Id.* at § 323, 52 Stat. at 907 (codified as 11 U.S.C. § 723 and repealed in 1978). *See also id.* at §§ 423, 623, 52 Stat. at 918, 932 (formerly 11 U.S.C. §§ 823, 1023) imposing identical insolvency requirements for, respectively, Chapter XII (real property arrangements for individual and partnership petitions) and Chapter XIII (wage earners' plans). Under the Reform Act, equity sense insolvency (defined as a failure to pay current debts as they become due) is a requirement for involuntary bankruptcy relief under both Chapters 7 and 11. *See* 11 U.S.C. § 303(h)(1) (1988).

8 We use the term "creative" bankruptcy in much the same sense that we believe Professor Kennedy used the term in his essay *Creative Bankruptcy? Use and Abuse of the Bankruptcy Law—Reflection on Some Recent Cases*, 71 IOWA L. REV. 199 (1985).

9 In addition to the implied good faith filing requirement which forms the basis of this Article, a few courts have denied Chapter 11 relief to individual, non-business debtors on the ground that Chapter 11 is designed exclusively for the reorganization of a business. *See In re* Toibb, 902 F.2d 14 (8th Cir. 1990), *cert. granted*, 111 S. Ct. 775 (1991); Wamsganz v. Boatmen's Bank of DeSoto, 804 F.2d 503 (8th Cir. 1986); *In re* Ponn Realty Trust, 4 Bankr. 226 (Bankr. D. Mass. 1980). However, most of the courts that have addressed the question point to the legislative history of the Reform Act as the basis for refusing to gloss such a limitation onto the language of the Code. *See, e.g., In re* Cook, 98 Bankr. 624, 625 (Bankr. D. Mass. 1989) (while Congress expected Chapter 11 to be used primarily by businesses, it did not rule out use of that chapter by individuals); *see also In re* Fund for a Conservative Majority, 100 Bankr. 307 (Bankr. E.D. Va. 1989); Warner v. Universal Guardian Corp. (*In re* Warner), 30 Bankr. 528 (Bankr. 9th Cir. 1983); Grundy Nat'l Bank. v. Shortt, 80 Bankr. 802 (W.D. Va. 1987).

Similarly, several courts of appeals have rejected the argument that the successive filing of Chapter 7 and 13 plans (so-called Chapter 20s, designed to take advantage of the benefits of Chapter 13 but first eliminate all dischargeable debt through an earlier Chapter 7 filing) is, standing alone, a sufficient basis to find bad faith. *See* Jim Walters Homes, Inc. v. Saylors (*In re* Saylors), 869 F.2d 1434 (11th Cir. 1989); Education Assistance Corp. v. Zellner, 827 F.2d 1222 (8th Cir. 1987); Downey Sav. & Loan Ass'n v. Metz (*In re* Metz), 820 F.2d 1495 (9th Cir. 1987); *In re* Chaffin, 816 F.2d 1070 (5th Cir. 1987), *on reh'g*, 836 F.2d 215 (1988); *cf.* Howe State Bank of Lewis v. Johnson (*In re* Johnson), 904 F.2d 563 (10th Cir. 1990) (refusing to confirm (albeit on grounds other than bad faith) a Chapter 13 plan that proposed to reschedule a mortgage obligation discharged in an earlier liquidation case), *cert. granted*, 111 S. Ct. 781 (1991).

10 The Chandler Act Amendments to the Bankruptcy Act added Chapter X governing corporate reorganizations. Act of June 22, 1938, ch. 575, 52 Stat. 840 (1938). Section 141 of the Bankruptcy Act (former 11 U.S.C. § 541) governed the filing of a reorganization petition under Chapter X. It expressly provided that "[u]pon the filing of a petition by a debtor, the judge shall enter an order approving the petition, if satisfied that it complies with the requirements of this chapter *and has been filed in good faith*, or dismissing it if not so satisfied." (emphasis added).

The courts implied a similar requirement for petitions filed under Chapters XI, XII, and XIII of the Bankruptcy Act. *See generally In re* Victory Constr. Co., 9 Bankr. 549, 557 (Bankr. C.D. Cal. 1981), *modified*, 9 Bankr. 570, *vacated as moot*, 37 Bankr. 222 (Bankr. 9th Cir. 1984); Comment, *Good Faith in Presenting Petitions for Reorganization Proceedings*, 37 MICH. L. REV. 912 (1939).

In 1970, Congress established the Commission on Bankruptcy Laws of the United States to "study, analyze, evaluate, and recommend changes" in existing bankruptcy law. Pub. L. No. 91-354, This judicially imposed good faith filing requirement has been thoroughly chronicled in commentary[11] and in the extensive case law. In this Article, we propose that the bankruptcy courts' adaptation of the good faith doctrine presents an excellent example of the law in evolution, a process we believe to be describable in meaningful terms from the positive law of the cases. With this as our working assumption, good faith is transformed from a tired cliché, invoked in suspicious response to an array of novel filings, to a useful instrument pressed into service by the courts to bring order and standards to the business of assuring that bankruptcy policy and purposes evolve in a sensible, purposeful way.

To declare good faith to be the device which, in the hands of the judiciary, moderates the evolution of bankruptcy purposes and policy is one thing; to offer a useful descriptive model with which to analyze and understand the device and the manner of its operation is quite another. Accordingly, the object of this Article is to cast light upon the nature of the good faith doctrine and its place in the evolutionary process. To this end, this Article is divided into three parts.

In Part I, we analyze the good faith doctrine as it has evolved and been applied in the case law to date. Through this process, we are able to

---

84 Stat. 468 (1970). The Commission's work was the basis for several proposed bankruptcy reform bills, including the bill that was eventually enacted into law in 1978. In its 1973 report, the Commission recommended the deletion of an express good faith requirement on the basis that it was premature for the court to determine at filing whether or not bad faith existed. H.R. DOC. NO. 137, 93d Cong., 1st Sess. 183, 222-23 & n.7 (1973). The Commission cited the right of creditors to seek dismissal or conversion to liquidation upon a showing that it is unreasonable to expect that a plan can be effected as an adequate control on futile cases. *Id.* While this arguably addressed the case of an objectively hopeless filing, the Commission apparently did not focus on the impact that elimination of an express good faith requirement would have on the viable but improperly motivated case. However, from very early on, courts recognized that the power to screen for and appropriately respond to bad faith in filing was implicit in the general equitable powers of the court. *See generally* Little Creek Dev. Co. v. Commonwealth Mortgage Co. (*In re* Little Creek Dev. Co.), 779 F.2d 1068, 1072 (5th Cir. 1986) ("Such a standard [good faith] furthers the balancing process between the interests of debtors and creditors which characterizes so many provisions of the bankruptcy laws and is necessary to legitimize the delay and costs imposed upon parties to a bankruptcy."); *Victory Constr. Co.*, 9 Bankr. at 558 (Bankr. C.D. Cal. 1981) ("It would be more than anomalous to conclude that . . . Congress [by failing to incorporate an explicit good faith requirement] intended to do away with a safeguard against abuse and misuse of process which had been established and accepted as part of bankruptcy philosophy . . . for almost a century.").

11 *See, e.g.*, Bacon & Spies, *Bad Faith Bankruptcies*, 26 HOUS. LAW. 33 (1989); Cohn, *Good Faith and the Single-Asset Debtor*, 62 AM. BANKR. L.J. 131 (1988); DiDonato, *Good Faith Reorganization Petitions: The Back Door Lets the Stranger In*, 16 CONN. L. REV. 1 (1983); DiPietro & Katz, *Chapter 11 of the Bankruptcy Code—Use or Abuse?*, 57 CONN. B.J. 418 (1983); Gaffney, *Bankruptcy Petitions Filed in Bad Faith: What Actions Can Creditor's Counsel Take?*, 12 U.C.C. L.J. 205 (1980); Kennedy, *supra* note 8; Ordin, *The "Good Faith" Principle in the Bankruptcy Code: A Case Study*, 38 BUS. LAW. 1795 (1983); Note, *Good Faith Inquiries Under the Bankruptcy Code; Treating the Symptom, Not the Cause*, 52 U. CHI. L. REV. 795 (1985) [hereinafter Note, *Good Faith Inquiries Under the Bankruptcy Code*]; Note, *Good Faith in Chapter Eleven Reorganizations*, 35 S.C.L. REV. 333 (1984); Note, Manville: *Good Faith Reorganization or "Insulated Bankruptcy"*, 12 HOFSTRA L. REV. 121 (1983) [hereinafter Note, Manville: *Good Faith Reorganization*].

identify and differentiate three categories of cases in which courts have grappled with the scope and operation of the good faith filing requirement. We conclude Part I by suggesting that good faith has come to function as the vehicle by which the purposes of the bankruptcy process are tested and advanced.

The suggestion that concludes Part I then raises the question, what are the purposes of bankruptcy law? This question leads to our examination in Part II of current scholarly discourse on the theoretical underpinnings of bankruptcy, followed by our attempt to relate that discourse to our discussion of good faith. Part II ends with a statement of our own jurisprudential assumptions concerning the evolution of legal doctrine and policy.

In Part III, our broad assumptions from Part II are translated into guiding principles for exposition of the case law discussed in Part I. Having in mind the formulation of a working theory of good faith's role in developing bankruptcy policy, our survey of the decisions leads us to derive a simple calculus as an aid to understanding the good faith cases. Each category of cases described in Part I is reconsidered from the perspective of the calculus. Finally, to illustrate its practical usefulness, we indulge in applications of the calculus under hypothetical assumptions that implicate novel or questionable uses of federal bankruptcy law. Through this process, we propose not simply a framework for evaluating the outcomes of particular cases, but also a fresh outlook from which to reflect upon the future course of bankruptcy policy.

I. The Good Faith Filing Requirement in the Case Law

A. *Background*

The Fourth Circuit Court of Appeals' decision in *Carolin Corp. v. Miller*[12] is representative of the kind of analysis that the courts have used in addressing the good faith filing issue.

The court initially observed that a threshold good faith obligation is necessary to protect the jurisdictional integrity of the bankruptcy courts.[13] In addition, the court pointed out that the "for cause" language in Code sections 1112(b)[14] and 362(d)[15] implicitly invites inquiry into the

12 886 F.2d 693 (4th Cir. 1989). This was a case of first impression in the Fourth Circuit.

13 *Id.* at 698. The court noted that, despite the lack of express authorization in the statute, courts presented with the question consistently had recognized bad faith as cause for dismissal.

14 11 U.S.C. § 1112(b) (1988) allows the bankruptcy court to convert or dismiss a Chapter 11 case "for cause," and lists circumstances that may constitute cause, including the absence of a reasonable likelihood of rehabilitation, inability to effectuate a plan, and prejudicial delay. 11 U.S.C. § 1112(b)(1)-(3). That provision's legislative history, however, makes clear that the enumerated circumstances are non-exclusive and that the bankruptcy court, relying upon its equitable powers, might consider other factors as grounds for dismissal in individual cases. H.R. REP. No. 595, 95th Cong., 2d Sess. 406, *reprinted in* 1978 U.S. CODE CONG. & ADMIN. NEWS 5963, 6362.

In a dissenting opinion, Judge Widener urged that, before dismissing the case on the basis of debtor's good faith as a necessary incident to the proper application of those provisions,[16] and that Bankruptcy Rule 9011[17] forms a clear basis for implying a good faith requirement in all bankruptcy pleadings, including Chapter 11 petitions.[18]

Having established the bankruptcy courts' authority to summarily dismiss bad faith petitions, the court turned its attention to the standards by which the exercise of this power is to be governed. It identified two distinct approaches. Some courts hold that sufficient grounds for dismissal exist when *either* objective futility or subjective bad faith can be shown.[19] Other courts apply a more demanding test, requiring a demonstration of *both* the inability to formulate an effective reorganization plan and improper motivation in filing.[20] Citing the harsh repercussions of denying threshold access to Chapter 11 relief, the majority in *Carolin* concluded that the more stringent test better serves the "various and con-

---

questionable extra-statutory filing limitations, the proper course would have been to remand for consideration of whether dismissal might be warranted under the express provisions of § 1112(b). *Carolin*, 886 F.2d at 707, 708 (Widener, J., dissenting).

15 11. U.S.C. § 362(d) (1988) permits creditors to obtain relief from the automatic stay "for cause." Section 362(d) does not expressly define "cause" to include lack of good faith. Nevertheless, as in the case of dismissal under § 1112(b), numerous cases have so held. *See, e.g.*, authorities cited in Little Creek Dev. Co. v. Commonwealth Mortgage Co. (*In re* Little Creek Dev. Co.), 779 F.2d 1068, 1072 n.2 (5th Cir. 1986); Natural Land Corp. v. Baker Farms, Inc. (*In re* Natural Land Corp.), 825 F.2d 296 (11th Cir. 1987); Acquisition Corp. of Am. v. Federal Savs. & Loan Ins. Corp., 96 Bankr. 380 (S.D. Fla. 1988); Canadian Imperial Bank of Commerce v. Oklahoma P.A.C. First Ltd. Partnership (*In re* Oklahoma P.A.C. First Ltd. Partnership), 122 Bankr. 394 (Bankr. D. Ariz. 1990); *In re* Colonial Manor Assocs., 103 Bankr. 315 (Bankr. M.D. Fla. 1989); Sentry Bank and Trust Co. v. Goulding Place Developers, Inc. (*In re* Goulding Place Developers, Inc.), 99 Bankr. 493 (Bankr. N.D. Ga. 1989); *In re* Missouri Flats Assocs., 86 Bankr. 634 (Bankr. E.D. Cal. 1988).

16 The court reasoned that since the granting of relief from stay in a single-asset, one-creditor case would normally be followed by outright dismissal in due course, "the statute inferentially permits inquiry into the debtor's good faith in commencing the case as a whole." *Carolin*, 886 F.2d at 699. For an in-depth discussion of the concept of good faith as applied in a variety of contexts under the Bankruptcy Code, see Ordin, *supra* note 11.

Other courts have pointed to the inherent equitable power of the bankruptcy courts under 11 U.S.C. § 105(a) (1988) as another source of implicit authority for the power to impose a good faith filing requirement. *See, e.g.*, *In re* Hartford Run Apts. of Buford, Ltd., 102 Bankr. 130, 132 (Bankr. S.D. Ohio 1989); Continental Ill. Nat'l Bank & Trust Co. v. Century City, Inc. (*In re* Century City, Inc.), 8 Bankr. 25 (D.N.J. 1980); *see also* 11 U.S.C. § 305 (1988) which permits the bankruptcy court to dismiss a case when to do so would be in the best "interests of creditors and the debtor."

17 FED. R. BANKR. P. 9011, which is an adaption of FED. R. CIV. P. 11, provides, among other things, that the signature of an attorney or a party to any paper served or filed in a case constitutes a certification that the pleading has not been interposed for frivolous, dilatory, or improper purposes, and that the contents thereof are well grounded in fact. Thus, by its terms, Bankruptcy Rule 9011 requires both a reasonable objective basis for the averments made in any pleading and subjective good faith.

18 *Carolin*, 886 F.2d at 700 ("Rule 9011 necessarily implies that all bankruptcy pleadings, including Chapter 11 petitions, must be filed in good faith.").

19 *Id.*

20 *Id.*

flicting interests of debtors, creditors and the courts."[21]

The court next considered the evidence required to establish each element of this two-pronged inquiry into good faith. While clearly regarding ability to reorganize and motive as requiring separate inquiries, the court recognized that proof of the two would frequently overlap,[22] even to the point that proof of an inability to effectuate a reorganization plan might be so overwhelming as to lead inescapably to an inference of subjective bad faith.[23]

If it appreciated the need for more by way of substantive direction in the good faith analysis, the *Carolin* majority nevertheless reverted to the shopworn litany that satisfaction of the good faith requirement can only be measured by a "totality of circumstances" inquiry,[24] "to determine whether the purposes of the Code would be furthered by permitting the

[21] *Id.* at 701. Given the court's reliance on Bankruptcy Rule 9011 as evidence of an implicit power in the Code to dismiss for bad faith in filing, it is arguable that adoption of the *less* stringent test may have been the more justifiable standard, inasmuch as *either* an improper purpose or an inadequately supportable or frivolous assertion may give rise to sanctions under Rule 9011. *See generally In re* McDonald Trucking Co., 76 Bankr. 513, 516 (Bankr. W.D. Pa. 1987) (Rule 9011 encompasses both an improper purpose and an improper use test); Byrne, *Sanctions for Wrongful Bankruptcy Litigation*, 62 AM. BANKR. L.J. 109, 114 (1988).

An interesting analogy can be drawn to the interpretation of the explicit "good faith" provision at 11 U.S.C. § 303(i)(2) (1988), which governs the right to recovery of actual and punitive damages for involuntary bankruptcy cases found to have been initiated in bad faith. For a time, there was a split in the cases over whether to measure bad faith by an objective standard of what a reasonable creditor in the position of the petitioning creditor would have done, or by a subjective test focusing on the petitioning creditor's motives for initiating the filing. *See* S. SNYDER & L. PONOROFF, COMMERCIAL BANKRUPTCY LITIGATION § 5.14 (1989, 1990-91). Increasingly, however, courts have considered both objective and subjective factors in determining whether bad faith exists. *See, e.g.*, U.S. Fidelity & Guar. Co. v. DJF Realty & Suppliers, Inc., 58 Bankr. 1008, 1012 (N.D.N.Y. 1986); Basin Elec. Power Coop. v. Midwest Processing Co., 47 Bankr. 903, 909 (D.N.D. 1984), *aff'd*, 769 F.2d 483 (8th Cir. 1985), *cert. denied*, 474 U.S. 1083 (1986); *see also In re* Johnston Hawks, Ltd., 72 Bankr. 361, 367 n.2 (Bankr. D. Haw. 1987) (suggesting that, in the final analysis, the objective test is really a subjective one since the question of whether a party acted in bad faith is a question of fact to be decided by the court). More recently, some courts have proposed that the test of bad faith under § 303(i)(2) should be identical to the standards contained in FED. R. BANKR. P. 9011. *See In re* Better Care, Ltd., 97 Bankr. 405, 410-12 (Bankr. N.D. Ill. 1989); *In re* Tarasi & Tighe, 88 Bankr. 706, 710-12 (Bankr. W.D. Pa. 1988); *In re* Turner, 80 Bankr. 618, 623 (Bankr. D. Mass. 1987).

[22] *Carolin*, 886 F.2d at 701. For example, because of the inherent difficulties associated with proving subjective intention, improper motivation might be inferred from evidence of objective futility.

[23] *Id.* at n.3. While this proposition is entirely reasonable given the practical limitations of proving state of mind other than indirectly, it is not entirely clear from the court's logic that it would consider the converse proposition true as well: in other words, could proof of an improper purpose in a given case be so manifest that it could alone support a parallel finding of objective futility? The court in *Carolin* seemed to acknowledge this possibility, at least in theory. *Id.* at 701. Nevertheless, a test that requires that *both* objective futility and subjective bad faith be evident would seem to stretch beyond the bounds of reason.

[24] *See id.* at 701 ("We simply note, as have other courts, that a totality of circumstances inquiry is required.").

Chapter 11 petitioner to proceed past filing."[25] Unassailable as a matter of principle, such broad admonitions offer little practical guidance. This is not seriously to criticize the opinion of the court in *Carolin*.[26] Rather, it is to emphasize that the good faith requirement serves a more fundamental purpose in bankruptcy than is evident in the decisions and literature to date. To provide a framework for addressing that broader question of purpose, it is useful first to examine the types of cases that have given rise to good faith challenges.

B. Categories of Good Faith Cases

Three broad patterns of conduct implicate good faith concerns in Chapter 11 filings:[27] (1) the one-asset (usually real estate) debtor case; (2) resort to bankruptcy court protection in order to make strategic use of a specific bankruptcy law right or power; and (3) use of bankruptcy to secure a tactical litigation advantage. We shall examine each.

1. *The One-Asset Debtor Scenario*—The facts of *Carolin* illustrate the one-asset debtor case.[28] This pattern of conduct, involving an eve-of-foreclosure filing by a debtor whose primary asset consists of troubled collateral, has recurred frequently enough in recent years to earn its own moniker, the "new debtor syndrome."[29] The cases and literature use this

---

[25] *Id.* In *Carolin*, the court found what it termed "abundant direct and circumstantial evidence in the record to support the bankruptcy court's conclusion that Carolin filed its petition for impermissible purposes," involving, primarily, an intention to hold a single asset "hostage" from a secured creditor's collection efforts while speculating (all at the creditor's risk) on sufficient appreciation to recover the value of the original investment in that asset. *Id.* at 703-05.

[26] In fairness, the court pointed out the danger that results from forcing particular facts into previously identified patterns of conduct. *Id.* at 705. We agree that this danger is very real. *See infra* note 27.

[27] *But cf. infra* text accompanying notes 176-78, concerning the limitations and inherent arbitrariness involved in this or, for that matter, any other scheme for arranging factually disparate cases by class or category. Despite these limitations, such groupings, even if highly artificial, are useful conventions to facilitate discussion of basic issues and provide a framework for further analysis. Thus, we submit to the temptation of grouping the cases into broad categories, but remain mindful that the factual mix in the actual cases is a much more kaleidoscopic affair than any such taxonomic approach would tend to indicate.

[28] The corporate debtor's principal asset was a single parcel of land subject to a deed of trust given to secure the original acquisition financing for the property. The property was not producing income at the time of the Chapter 11 filing, and the debtor had no other ongoing business operations. Moreover, on the same day as the filing, all the outstanding capital stock of the debtor was acquired by new owners. Curiously, the purchaser of the troubled corporation's stock was a newly formed company. Two of its principals had previously owned the land and building now constituting Carolin's principal asset. The filing itself preceded by less than one hour a scheduled foreclosure sale of the debtor's property. Finally, after commencement of the case, it was the trust deed beneficiary who filed the motion to dismiss, or in the alternative for relief from stay. *Carolin*, 886 F.2d at 695-96.

[29] *See In re* N. R. Guaranteed Retirement, Inc., 112 Bankr. 263, 273 n.8 (Bankr. N.D. Ill.), *aff'd*, 119 Bankr. 149 (N.D. Ill. 1990); *In re* Victory Constr. Co., 9 Bankr. 549 (Bankr. C.D. Cal. 1981), *modified*, 9 Bankr. 570, *vacated as moot*, 37 Bankr. 222 (Bankr. 9th Cir. 1984); Ordin, *supra* note 11, at 1813-27. In some cases, however, pre-bankruptcy transfer of the property facing foreclo-

label to refer to the isolation of property subject to impending foreclosure in a shell entity, usually but not always of recent origin.[30] While the factual pattern varies to some degree from case to case, all of these filings share a common feature. In each, the debtor lacks most or all of the customary trappings of a regular and significant business enterprise—namely, unsecured creditors, employees, customers, and inventory.[31]

The absence of any ongoing business, especially when combined

---

sure was accomplished for the apparent purpose of moving assets from an entity or ownership arrangement statutorily proscribed from seeking bankruptcy relief to a corporation. *See, e.g., In re* 299 Jack-Hemp. Assocs., 20 Bankr. 412 (Bankr. S.D.N.Y. 1982) (property transferred from a probate estate); *In re* G-2 Realty Trust, 6 Bankr. 549 (Bankr. D. Mass. 1980) (transfer from ineligible non-business trust to a corporation). *See generally* 11 U.S.C. § 109 (1988) (eligibility to seek bankruptcy relief); *supra* note 7.

This label also may be something of a misnomer to the extent it has come to be used to describe cases in which there was no actual pre-bankruptcy "transfer" of the collateral as well as cases involving newly formed entities. *Carolin* is an example of a case described by the court as fitting the "new debtor syndrome" fact pattern but in which no recent transfer of assets had occurred. *See supra* note 28. Actually, the factor which these cases most often have in common is a single or single dominant-asset debtor without regular and ongoing business activities and operations. *See, e.g.*, Phoenix Picadilly, Ltd. v. Life Ins. Co. of Va. (*In re* Phoenix Picadilly, Ltd.), 849 F.2d 1393 (11th Cir. 1988) (filing by limited partnership owner of apartment building dismissed as having been undertaken solely to delay and frustrate the legitimate collection efforts of secured creditors). Therefore, we prefer the term "one-asset debtor" filing to describe this type of case, but acknowledge the prevalence of the "new debtor syndrome" tag.

30 The classical "new debtor syndrome" case involves the transfer of distressed property to a newly formed or revitalized entity shortly before the filing for bankruptcy. *See supra* note 29. In such a case, the transferee's intention is to protect other assets in which substantial equity may exist. Cases falling into this category include: Natural Land Corp. v. Baker Farms, Inc. (*In re* Natural Land Corp.), 825 F.2d 296, 297 (11th Cir. 1987) (property transferred from individuals to a shell corporation on the day state court judgment of foreclosure was ordered); Meadow Brook Investors v. Thirtieth Place, Inc. (*In re* Thirtieth Place, Inc.), 30 Bankr. 503, 504-05 (Bankr. 9th Cir. 1983) (debtor formed for predominant purpose of filing for bankruptcy); Canadian Imperial Bank of Commerce v. Oklahoma P.A.C. First Ltd. Partnership (*In re* Oklahoma P.A.C. First Ltd. Partnership), 122 Bankr. 394, 402-03 (Bankr. D. Az. 1990) (decided under 11 U.S.C. §§ 362(d), 1112(b)); *In re* Meyers Way Dev., Ltd., 116 Bankr. 239, 240-41 (Bankr. W.D. Wash. 1990) (property transferred from cotenancy to limited partnership); *In re* The Ophir Trust, 112 Bankr. 956, 958 (Bankr. E.D. Wis. 1990) (historic mansion transferred from individual owner to trust naming grantor as sole beneficiary); *In re* Eighty South Lake, Inc., 63 Bankr. 501, 507 (Bankr. C.D. Cal. 1986) (transferee corporation was formed eight months prior to filing, but inactive for most of that time), *aff'd*, 81 Bankr. 580 (Bankr. 9th Cir. 1987); California Mortgage Serv. v. Yukon Enters. (*In re* Yukon Enters.), 39 Bankr. 919, 920 (Bankr. C.D. Cal. 1984) (transfer of only financially troubled property, in close proximity to filing, to newly formed corporation); *In re* Dutch Flat Inv. Co., 6 Bankr. 470, 471 (Bankr. N.D. Cal. 1980) (transfer to newly formed subsidiary accomplished to avoid subjecting assets of parent companies to jurisdiction of the bankruptcy court).

31 *In re* Winshall Settlor's Trust, 758 F.2d 1136, 1137 (6th Cir. 1985) (requirement of an ongoing business is inherent in Chapter 11); *Ophir*, 112 Bankr. at 959-60. Some courts have gone as far as to hold that individual debtors without an ongoing business enterprise are per se ineligible to seek Chapter 11 relief. *See, e.g.*, Wamsganz v. Boatman's Bank of DeSoto, 804 F.2d 503 (8th Cir. 1986). Most courts, however, stop short of a blanket prohibition, recognizing a place for non-business reorganizations. *See, e.g.*, Gonzales v. Parks, 830 F.2d 1033, 1034 n.1 (9th Cir. 1987); *In re* Grundy Nat'l Bank v. Shortt, 80 Bankr. 802 (W.D. Va. 1987); *In re* Cook, 98 Bankr. 624 (Bankr. D. Mass. 1989); *see also supra* note 9.

with a lack of any apparent equity in the debtor's single asset,[32] make the prospects for a successful reorganization in these cases slim indeed. Thus, many courts have inferred that the one-asset debtor's true motivation for seeking Chapter 11 protection is to delay exercise of secured creditors' legitimate state law rights and remedies against the collateral.[33] The suspicion is that, by gaining some breathing space through a reorganization proceeding, the debtor is looking not to rehabilitate a business, but to alleviate its financial crunch through hoped-for appreciation in the value of its encumbered property.[34] Similarly, during an inflationary period, the one-asset debtor may file for bankruptcy in order to pre-

[32] In Phoenix Picadilly, Ltd. v. Life Ins. Co. of Va. (*In re* Phoenix Picadilly, Ltd.), 849 F.2d 1393, 1395 (11th Cir. 1988), the court held that the existence of apparent equity in the debtor's property does not conclusively rebut an assertion of bad faith in filing. *See also In re* Meyers Way Dev. Ltd., 116 Bankr. 239, 245 (Bankr. W.D. Wash. 1990) (value of property is not an issue once bad faith is established); *cf. In re* Tiffany Square Assocs., 104 Bankr. 438, 442 (Bankr. M.D. Fla. 1989) (rejecting the suggestion that *Phoenix Picadilly* stands for the proposition that the existence of equity is irrelevant in determining whether a filing was in good faith).

[33] *See Phoenix Picadilly*, 849 F.2d at 1394; Albany Partners, Ltd. v. Westbrook (*In re* Albany Partners, Ltd.), 749 F.2d 670, 674 (11th Cir. 1984). Other cases falling into this category include: Meadowbrook Investors' Group v. Thirtieth Place, Inc. (*In re* Thirtieth Place), 30 Bankr. 503 (Bankr. 9th Cir. 1983); *In re* The Ophir Trust, 112 Bankr. 956 (Bankr. E.D. Wis. 1990); *In re* Castleton Assocs., 109 Bankr. 347 (Bankr. S.D. Ind. 1989); *In re* Walter, 108 Bankr. 244 (Bankr. C.D. Cal. 1989); *In re* Stulley, 108 Bankr. 174 (Bankr. S.D. Ohio 1989); Home Fed. Savs. v. Club Candlewood Assocs. (*In re* Club Candlewood Assocs.), 106 Bankr. 752 (Bankr. N.D. Ga.), *appeal dismissed*, 106 Bankr. 758 (N.D. Ga. 1989); *In re* U.S. Loan Co., 105 Bankr. 676 (Bankr. M.D. Fla. 1989) (decided under § 1112(b)); *In re* Berkshire Manor Apts., Ltd., 104 Bankr. 417 (Bankr. N.D. Fla. 1989) (decided under § 1112(b)); *In re* Adkinson, 94 Bankr. 730 (Bankr. N.D. Fla. 1988); *In re* Citadel Properties, Inc., 86 Bankr. 275 (Bankr. M.D. Fla. 1988); *In re* Randy Homes Corp., 86 Bankr. 259 (Bankr. M.D. Fla. 1988); *In re* Brandywine Assocs., 85 Bankr. 626 (Bankr. M.D. Fla. 1988); *In re* Wentworth, 83 Bankr. 705 (Bankr. D.N.D. 1988); *In re* Forest Activities, Ltd., 81 Bankr. 720 (Bankr. S.D. Fla. 1988); *In re* Southern Cal. Sound Systems, Inc., 69 Bankr. 893 (Bankr. S.D. Cal. 1987); *In re* Sar-Manco, Inc., 70 Bankr. 132 (Bankr. M.D. Fla. 1986); *In re* Volpe, 53 Bankr. 46 (Bankr. M.D. Fla. 1985); Glassmanor Apts. Ltd. Partnership v. Corporation Deja Vu (*In re* Corporation Deja Vu), 34 Bankr. 845 (Bankr. D. Md. 1983); North Cent. Dev. Co. v. Landmark Capital Co. (*In re* Landmark Capital, Co.), 27 Bankr. 273 (Bankr. D. Ariz. 1983); Polkin, Inc. v. Lotus Inv., Inc. (*In re* Lotus Inv., Inc.), 16 Bankr. 592 (Bankr. S.D. Fla. 1981).

[34] In Natural Land Corp. v. Baker Farms, Inc. (*In re* Natural Land Corp.), 825 F.2d 296, 299 n.1 (11th Cir. 1987), the debtor argued that, because of an increase in the value of the underlying property, the secured creditors that had moved for dismissal had not been harmed by the allegedly bad faith filing. The court rejected this contention as frivolous, noting: "Plainly stated, Natural Land abused the bankruptcy process when it used the automatic stay provision to bide time, in the hope that the value of the foreclosed property would rise and produce a windfall profit." *Id.* Similarly, in *In re* American Property Corp., 44 Bankr. 180, 182 (Bankr. M.D. Fla. 1984), the court identified the debtor's objective in the paradigm bad faith case as holding a single asset "hostage" in the hope "that such asset may increase in value" sufficiently for the debtor to "recover its original investment [all] at the creditor's risk." *Accord Carolin*, 886 F.2d at 705 (Chapter 11 filing designed to use bankruptcy protections for risk-free speculation in a single asset amounted to bad faith); *In re* Castleton Assocs., 109 Bankr. 347, 351 (Bankr. S.D. Ind. 1989) (debtor improperly sought to avoid the consequences of its bad judgment and pass the loss and risk on to the secured creditor who would not share in the value of any future appreciation).

serve the value of below-market financing on its property.[35]

Unquestionably, most of the law regarding the implied good faith filing requirement has been developed in reorganization proceedings involving debtors falling into this broadly defined one-asset or new debtor syndrome category. Over the past several years, the number of reported cases has become legion.[36] In the bulk of these cases, the good faith challenge has come from frustrated secured creditors. Nevertheless, because the good faith issue also involves the question of whether its jurisdiction has been properly invoked, the bankruptcy court may raise the issue on its own motion.[37]

In either case, to detect bad faith in one-asset debtor cases most

---

[35] Generally, in a Chapter 11 case a debtor-in-possession can preserve the benefit of a below-market rate loan by curing any pre-petition default, and, notwithstanding the existence of an acceleration clause in the instrument creating the debt, can reinstate the original payment schedule and maturity date. *See* 11 U.S.C. §§ 1124(1), 1129(a)(8)(B) (1988). Moreover, even if a plan of reorganization is never confirmed, the filing itself operates to stay all foreclosure efforts. *See generally* 11 U.S.C. § 362(a); S. SNYDER & L. PONOROFF, *supra* note 21, at §§ 6.01-.03. While the stay is in effect, unless the creditor is oversecured, interest does not accrue on the creditor's claim against the debtor. 11 U.S.C. § 506(b). An undersecured creditor is entitled to adequate protection of its interest in property of the estate while the stay is in effect. 11 U.S.C. §§ 361, 362(d)(1). However, in United Savs. Ass'n of Tex. v. Timbers of Inwood Forest Assocs., 484 U.S. 365 (1988), the Supreme Court rejected the argument that undersecured creditors have a right to post-petition interest or adequate protection to compensate them for the lost opportunity cost occasioned by the delay resulting from the stay. Thus, a secured creditor in a single asset case, at best, can expect to lose the difference between market and stated rates of interest during the pendency of the case, and, at worst, could lose all time value of money until it obtains relief from the stay or the case is dismissed.

In Yaffee v. Andrews (*In re* Andrews), 17 Bankr. 515, 518-19 (Bankr. C.D. Cal. 1982), the court held that a filing motivated primarily by a desire to preserve low-interest financing was subject to dismissal for bad faith. However, since the court in *Yaffee* also found that there was neither an ongoing business nor going concern value to preserve, the importance to the decision of the debtor's intent to take advantage of a low-interest loan is unclear. In any event, since *Timbers*, it would seem difficult to argue successfully for dismissal based on undercompensation of secured creditors alone.

[36] *See supra* notes 29 & 33 and authorities cited therein. This may be due, in part, to a deteriorating national real estate market.

In several instances, the bankruptcy courts have imposed sanctions on parties found to have filed in bad faith. *See* Midwest Properties No. Two v. Big Hill Inv. Co., 93 Bankr. 357, 361-62 (N.D. Tex. 1988); *In re* EPCO Northeast, Inc., 118 Bankr. 267, 269-70 (Bankr. E.D. Pa. 1990) (sanctions imposed on corporate debtor's president and counsel where debtor was a mere shell and no legitimate reorganization purpose existed); *In re* Cedar Falls Hotel Properties, Ltd., 102 Bankr. 1009, 1019-20 (Bankr. N.D. Ia. 1989) (appropriate to sanction corporate debtor's principal and his attorney for bad faith filing of Chapter 11 petitions); *In re* King, 83 Bankr. 843, 847 (Bankr. M.D. Ga. 1988) (sanctions imposed when filing was undertaken without a reasonable expectation of reorganization). *But see In re* Park Place Assocs., 118 Bankr. 613, 618 (Bankr. N.D. Ill. 1990) (standards for dismissing a case for lack of good faith are different than the improper purpose standard for imposing sanctions under Bankruptcy Rule 9011); *In re* HBA East, Inc., 101 Bankr. 411, 416-18 (Bankr. E.D.N.Y. 1989) (the lack of clear and uniform good faith filing standards augurs against adoption of a per se rule imposing sanctions in all bad faith dismissal cases).

[37] Little Creek Dev. Co. v. Commonwealth Mortgage Corp. (*In re* Little Creek Dev. Co.), 779 F.2d 1068, 1071 n.1 (5th Cir. 1986); Connell v. Coastal Cable T.V., Inc. (*In re* Coastal Cable T.V., Inc.), 709 F.2d 762, 764 (1st Cir. 1983) (matters relating to the bankruptcy court's jurisdiction may be raised *sua sponte*).

courts follow the same type of detailed, fact-based analysis undertaken in *Carolin*.[38] This analysis focuses on what the Fifth Circuit has termed various recurring but non-exclusive circumstances or badges of bad faith.[39] The courts have not, however, articulated any generalized set of methodological guidelines or normative touchstones which might be used to apply these factors in particular cases. Instead, the determination has been left to the bankruptcy judge's "on-the-spot evaluation" of the debtor's financial situation, motives, and prospects for obtaining the capital necessary for a confirmable plan of reorganization.[40]

Certainly, the courts have not censured all filings that fit the one-asset debtor pattern.[41] Even on the eve of foreclosure, the filing of a one-asset debtor's reorganization petition does not alone assure a finding of bad faith.[42] Indeed, some courts have observed that only when the evi-

---

38 *See supra* notes 24-25 and accompanying text.

39 *Little Creek*, 779 F.2d at 1072-73. The Fifth Circuit Court of Appeals identified these circumstances as including the now familiar pattern of a one-asset debtor with few unsecured creditors, no employees, and little or no cash flow, and subject to impending foreclosure by secured creditors. *Id.* at 1073. Other cases that have attempted to enumerate the indicia of an abusive filing include: Canadian Imperial Bank of Commerce v. Oklahoma P.A.C. First Ltd. Partnership (*In re* Oklahoma P.A.C. First Ltd. Partnership), 122 Bankr. 394, 402-03 (Bankr. D. Az. 1990) (identifying eight badges of bad faith); *In re* Walter, 108 Bankr. 244, 247 (Bankr. C.D. Cal. 1989) (identifying 10 common conditions which indicate bad faith); *In re* Ravick Corp., 106 Bankr. 834, 843-50 (Bankr. D.N.J. 1989); *In re* Wentworth, 83 Bankr. 705, 707 (Bankr. D.N.D. 1988) (14 factors); Northwest Place, Ltd. v. Cooper (*In re* Northwest Place, Ltd.), 73 Bankr. 978, 981 (Bankr. N.D. Ga. 1987) (same), *aff'd*, 108 Bankr. 809 (N.D. Ga. 1988); *In re* Hulse, 66 Bankr. 681, 682-83 (Bankr. M.D. Fla. 1986) (eight factors); *In re* Mildevco, Inc., 40 Bankr. 191, 194 (Bankr. S.D. Fla. 1984) (detailing facts suggestive of bad faith); California Mortgage Serv. v. Yukon Enters., (*In re* Yukon Enters.), 39 Bankr. 919, 921 (Bankr. C.D. Cal. 1984) (listing the seven indicia of bad faith in "new debtor" cases); Duggan v. Highland-First Avenue Corp., 25 Bankr. 955, 961 (Bankr. C.D. Cal. 1982) (listing several factors indicating bad faith).

This case-by-case approach to determining good faith based on the presence or absence of a non-exclusive list of criteria is quite similar to the approach several courts of appeals have taken in determining whether the express good faith requirement in 11 U.S.C. § 1325(a)(3) (1988) for confirmation of a Chapter 13 plan has been satisfied. *See, e.g.*, Pioneer Bank of Longmont v. Rasmussen (*In re* Rasmussen), 888 F.2d 703, 704-06 (10th Cir. 1989) (per se bad faith standard rejected in favor of a totality of circumstances approach); *In re* Smith, 848 F.2d 813, 818 (7th Cir. 1988); Downey Sav. & Loan Ass'n v. Metz (*In re* Metz), 820 F.2d 1495, 1498 (9th Cir. 1987); Kitchens v. Georgia R.R. Bank & Trust Co. (*In re* Kitchens), 702 F.2d 885, 888 (11th Cir. 1983); *In re* Estus, 695 F.2d 311, 316 (8th Cir. 1982).

40 *Little Creek*, 779 F.2d at 1072.

41 *See, e.g.*, Can-Alta Properties, Ltd. v. State Savs. Mortgage Co. (*In re* Can-Alta Properties), 87 Bankr. 89, 92 (Bankr. 9th Cir. 1988) (granting relief from stay on grounds of bad faith was improper despite presence of some indicia of one-asset debtor filing); Carteret Savs. Bank v. Nastasi-White, Inc. (*In re* East-West Assocs.), 106 Bankr. 767, 772 (S.D.N.Y. 1989) (bankruptcy court's finding of good faith would not be disturbed despite presence of some of the circumstances that normally evince a bad faith filing); *In re* N.R.G. Invests., 99 Bankr. 475, 476 (Bankr. M.D. Fla. 1989) (Chapter 11 case involving many of the "new debtor syndrome" criteria would not be dismissed in a situation where debtor had some equity in the property to preserve); *In re* Coral Springs Medical Center Assocs., 99 Bankr. 112 (Bankr. S.D. Fla. 1989); *see also infra* notes 43 & 44.

42 *See In re* Mill Place Ltd. Partnership, 94 Bankr. 139, 142 (Bankr. D. Minn. 1988).

dence is clear and convincing that the bankruptcy law is being used for the sole purpose of delaying or harassing a creditor does the debtor's conduct constitute an unlawful abuse of process.[43] Notwithstanding this styled sympathy for the interests of secured creditors, the courts' correlative emphasis upon the debtor's intent to injure or abuse the judicial process is revealing. It implies that, in defining lack of good faith in these cases, courts may be concerned less with mollifying beleaguered creditors than with what they perceive as attempts to pervert the judicial process by conscripting the courts as unwilling accomplices in a debtor's unsavory scheme to speculate on an investment asset at the expense of its secured creditors.[44]

[43] *Id.* at 141-42; *see also In re* Tiffany Square Assocs., 104 Bankr. 438, 441 (Bankr. M.D. Fla. 1989) (Judge Paskay stated: "there is nothing inherently improper in a single asset debtor filing a Chapter 11 Petition for Reorganization, even shortly before or after a foreclosure proceeding has commenced."); Cohn, *supra* note 11, at 136 n.15. In *Mill Place*, 94 Bankr. at 139, the court obviously placed the greatest emphasis on the debtor's malicious and hostile intent to harass and injure creditors. Other courts have shied away from a detailed assessment of the debtor's motivation in favor of a more objective test focusing on the realistic prospects for reorganization. *See, e.g., East-West Assocs.*, 106 Bankr. at 772 (the actual proposal of a plan was strong evidence of good faith); Mauna Lani Resort, Inc. v. Endrex Invs. (*In re* Endrex Invs.), 84 Bankr. 207, 210-11 (Bankr. D. Colo. 1988), *modified*, 111 Bankr. 939 (D. Colo. 1990); *In re* Sar-Manco, Inc., 70 Bankr. 132, 139 (Bankr. M.D. Fla. 1986).

Inevitably, however, motives enter into the calculus. *See Little Creek*, 779 F.2d at 1072. By commonly acknowledged definition, "good faith" connotes both subjective honesty and attention to reasonable standards of behavior and action. *See generally* Farnsworth, *Good Faith Performance and Commercial Reasonableness Under the Uniform Commercial Code*, 30 U. CHI. L. REV. 666, 667-71 (1963) (describing "good faith" in the commercial context as a "protean" concept involving both state of mind and performance tied to some objective standard of reasonableness). For further discussion of the general history and use of the good faith doctrine, particularly in the commercial context, see *infra* notes 168-172 and accompanying text.

It is worth interjecting at this point that most courts have taken the view that once a prima facie showing of bad faith has been made, the burden shifts to the debtor to show that continuation of the proceeding would not constitute an abuse of the bankruptcy system. *See In re* Meyers Way Dev. Ltd. Partnership, 116 Bankr. 239, 244-45 (Bankr. W.D. Wash. 1990) (once elements of "new debtor syndrome" have been shown, burden is on debtor to establish good faith business reason for the filing); *In re* N. R. Guaranteed Retirement, Inc., 112 Bankr. 263, 276 (Bankr. N.D. Ill. 1990) (upon a showing by a secured creditor that its collateral was transferred shortly before filing, Chapter 11 petition will be dismissed unless debtor proves lack of bad faith), *aff'd*, 119 Bankr. 149 (N.D. Ill. 1990); *In re* Hartford Run Apts. of Buford, Ltd., 102 Bankr. 130, 132 (Bankr. S.D. Ohio 1989); *In re* King, 83 Bankr. 843, 847 (Bankr. M.D. Ga. 1988); *In re* Business Information Co., 81 Bankr. 382, 385 (Bankr. W.D. Pa. 1988); *In re* Eighty S. Lake, Inc., 63 Bankr. 501, 508 (Bankr. C.D. Cal. 1986), *aff'd*, 81 Bankr. 580 (Bankr. 9th Cir. 1987).

[44] The truth of this assertion is confirmed upon considering one-asset cases where the debtor can show some arguable relation between the proposed reorganization and the broad policy of preserving going concern value which underlies Chapter 11. In these instances, notwithstanding that the actual harm to secured creditors may be no less than in those cases where the court concludes that the only hope of rehabilitation stems from, what the court in *Little Creek*, 779 F.2d at 1072, termed the debtor's own "terminal euphoria," courts have not typically second-guessed the decision to file. *See, e.g.*, Heisley v. U.I.P. Engineered Prods. Corp., 831 F.2d 54, 56 (4th Cir. 1987) (sound business reasons existed for corporate parent to seek Chapter 11 relief for its solvent subsidiaries); *In re* W. & L. Assocs., 71 Bankr. 962, 967-68 (Bankr. E.D. Pa. 1987) (proof of malice, serious misconduct or

2. *The Strategic Filing*—The second category of cases giving rise to good faith challenges involves petitions filed for the purpose of obtaining a particular benefit from one or more substantive provisions of the Bankruptcy Code. These cases typically involve a sizeable business enterprise seeking to manage a major, long-term business problem by means of an extraordinary bankruptcy power. They are, therefore, readily distinguishable from the standard one-asset debtor scenario.

Representative of cases falling in this category is the first Continental Airlines Corporation reorganization case, in which several of the company's unions filed a preliminary motion to dismiss on the ground that Continental had not filed its petition in good faith.[45] While Continental unquestionably had experienced serious financial difficulties in the several-year period before its filing, the unions pointed out that immediately after the filing Continental unilaterally imposed new wages and work rules on its employees and moved to reject its collective bargaining agreements.[46] Citing these actions, the unions argued that Continental's true motive for filing for bankruptcy was to evade its responsibilities under the federal labor laws.

The bankruptcy court disagreed, refusing to accept the proposition that a company otherwise in need of Chapter 11 relief should be declared ineligible simply because rejection of its labor contracts is contemplated as a component of its reorganization plan.[47] By emphasizing Continen-

dishonesty is necessary to establish bad faith); *In re* The Bible Speaks, 65 Bankr. 415, 425-26 (Bankr. D. Mass. 1986) (critical question is whether the debtor's use of the reorganization process bears some reasonable relation to the purposes of Chapter 11, citing *In re* Connell v. Coastal Cable T.V., Inc. (*In re* Coastal Cable T.V., Inc.), 709 F.2d 762, 764 (1st Cir. 1983)). The court in *Bible Speaks* also referred to legislative history in identifying the basic object of Chapter 11 as the need to return financially stressed businesses to economic viability thereby preserving jobs and assets. H.R. REP. No. 595, 95th Cong., 1st Sess. 220, *reprinted in* 1978 U.S. CODE CONG. & ADMIN. NEWS 5963, 6179; *see also infra* note 58 and accompanying text.

Similarly, in *East-West Assocs.*, 106 Bankr. at 772, the court sustained the bankruptcy court's finding that an involuntary filing was not in bad faith even though certain indicia of bad faith identified in Phoenix Picadilly, Ltd. v. Life Ins. Co. of Va. (*In re* Phoenix Picadilly, Ltd.), 849 F.2d 1393 (11th Cir. 1988), were present. The court observed that, while not dispositive, the petitioning creditors' ability to come forward with an effective plan of reorganization reflected favorably on the legitimacy of their motives and actions. *Id.*

[45] *In re* Continental Airlines Corp., 38 Bankr. 67 (Bankr. S.D. Tex. 1984). The unions' motion also alleged that approval of the debtor's motion to reject their collective bargaining agreements would violate the U.S. Constitution. *Id.* at 69.

[46] *Id.*

[47] *Id.* at 71. In the case before it, the court was obviously impressed and influenced by the company's demonstrated need for Chapter 11 relief in areas other than those relating to labor relations. The movants did not contest that, at the time of the filing, the corporation was experiencing a severe financial crisis; nor did they challenge the fact that Continental Airlines was on the verge of running out of cash with no reasonable source of additional capital or credit. Accordingly, the court concluded that the unions had not satisfactorily shown that the main purpose for the filing was other than the perfectly lawful one of keeping the company alive and viable. In fact, the court determined the facts to be specifically contrary to the unions' assertion. *Id.*

tal's recent financial woes, however, the court left open the possibility that a filing driven solely, or perhaps even primarily, by an intention to circumvent collective bargaining obligations might be vulnerable to dismissal for failure to satisfy the implied good faith requirement.[48]

The other major reported good faith decision involving a filing allegedly undertaken to secure a strategic advantage not obtainable outside of bankruptcy arose out of the Manville Corporation reorganization. In an opinion nearly contemporaneous with the *Continental Airlines* decision, the bankruptcy court likewise declined to dismiss the Manville Corporation's petition for lack of good faith in filing.[49] Led by a committee formed to represent litigants in asbestos-related suits against Manville,[50] the movants claimed the company had perpetrated a fraud by "concocting" evidence that exaggerated the extent of the financial distress resulting from the corporation's ongoing exposure to product liability claims.[51] The committee argued that Manville's true motive for initiating the bankruptcy proceeding was to take improper advantage of the discharge and claims estimation provisions of the Bankruptcy Code[52] in

---

[48] Thus, it is not clear whether the result might have been different if Continental, although ailing financially, had been found to have filed primarily for the purpose of taking advantage of the power of a Chapter 11 debtor to reject its collective bargaining agreements. In an article published shortly before the *Continental Airlines* decision, Professor Countryman had maintained that the Bankruptcy Code does not provide relief for a debtor whose only aim is to reject a labor contract. Countryman, *Is the National Labor Policy Headed for Bankruptcy?*, 1984 ANN. SURV. OF BANKR. L. 159 (Norton ed.); *see also In re* Southern Cal. Sound Systems, Inc., 69 Bankr. 893, 898-99 (Bankr. S.D. Cal. 1987) (where debtor's sole reason for filing for Chapter 11 relief was to reject an exclusive licensing contract, dismissal on bad faith grounds is warranted). *But see In re* Taylor, 103 Bankr. 511, 520-21 (D.N.J. 1989) (reorganization petition would not be dismissed for bad faith even where circumstances indicated that the real purpose for the filing was to reject contractual obligations); *In re* W. & L. Assocs., 71 Bankr. 962, 966-67 (Bankr. E.D. Pa. 1987) (filing a Chapter 11 petition solely for the purpose of rejecting an executory contract is not an abuse of bankruptcy process).

As discussed *supra* note 5, in response to the Supreme Court's decision in NLRB v. Bildisco & Bildisco, 465 U.S. 513 (1984), organized labor obtained some protection against rejection of collective bargaining agreements in bankruptcy as part of the Bankruptcy Amendments and Federal Judgeship Act of 1984. *See generally* Simon & Mehlsack, *Filing a Post-Bildisco Chapter 11 Petition to Reject a Labor Contract*, 52 FORDHAM L. REV. 1134 (1984); White, *supra* note 5.

[49] *In re* Johns-Manville Corp., 36 Bankr. 727 (Bankr. S.D.N.Y.) (issued Jan. 23, 1984, just six days after the *Continental Airlines* decision), *appeal denied*, 42 Bankr. 651 (S.D.N.Y.), *reh'g denied*, 42 Bankr. 654 (S.D.N.Y. 1984).

[50] The other parties supporting the motion to dismiss were co-defendants with Manville in various state court product liability suits. *Id.* at 729.

[51] *Id.* at 730. Manville had been required by its auditors to book a $1.9 billion contingency reserve for asbestos claims. Doing so resulted in the acceleration of hundreds of millions of dollars due under the terms of bank loan agreements and trust indentures. Thus, on paper, Manville presented a convincing picture of massive, unmanageable debt and cash flow crises. *Id.* at 738-40. However, the basis of the movants' challenge was that the accounting methods and data that had been used by Manville to create this image were manufactured and falsely distorted in order to erroneously present the appearance of just such a picture.

[52] Certainly Manville openly sought to deal with the continuing and open-ended problems of present and future asbestos-related claims by taking advantage of the Code's provisions for claims estimation, 11 U.S.C. § 502(c), and discharge, 11 U.S.C. § 1141(d). However, at the time the mo-

connection with a preconceived strategy designed to curtail the company's overall health liability costs.

In rejecting this contention, the court cited the apparently very real economic pressures imposed on Manville by virtue of the projected size of its future asbestos liability costs,[53] and determined that the debtor was wholly justified in electing to manage the ongoing business problems caused by the large number of asbestos health claims[54] through a single court-supervised reorganization rather than by the traditional means of

---

tions for dismissal were decided, the court had not indicated whether it would use its estimation power, and the question of dischargeability of the claims of future claimants had not been resolved. Ultimately, of course, Manville was able to affect such claims in the proceeding through the appointment of a legal representative for unknown putative product liability claimants. *See* Kane v. Johns-Manville Corp., 843 F.2d 636, 643-46 (2d Cir. 1988) (affirming the confirmation of Manville's plan of reorganization over the objection of asbestos-health claimants who had also sought to assert the rights of future asbestos-related personal injury claimants).

53 At the heart of the debate over Manville's financial soundness and its ability to meet its future liabilities other than by means of reorganization was the issue of whether Manville had properly booked a $1.9 billion reserve for contingent asbestos health liability claims. Ultimately, the court determined that the committee had failed to sustain its burden of proof of fraud as to either the amount or the necessity of booking the massive liability reserve. *Id.* at 735. Manville's justification was that it was following the advice of its independent auditors who, in turn, purported to be relying on uniformly accepted financial accounting standards.

Cases of large, public companies such as Manville, frequently involve questions of financial condition that are exceedingly complex. Resolution of these questions requires accounting judgments which the courts are ill-equipped and ill-disposed to make. Thus, the temptation is to defer, as the court did in *Manville*, to the professional judgment of members of the accounting profession. However, since questions about the application of accounting principles and standards in any given situation cannot be made with mathematical certainty or precision, and since reasonable accounting judgment can differ, it is virtually impossible in mega-reorganization cases to evaluate meaningfully the seriousness or immediacy of the company's financial pressures. As a result, substantive outcomes are often dictated simply by allocation of the burden of proof. The problem for courts in trying to develop a true picture of a company's financial condition is compounded by what are often the conservative biases built into accounting principles since, in presentation of financial information, greater emphasis is placed on uniformity in preparation than on reflection of absolute or "true" asset values. At the same time, alternative accounting methods can produce disparate financial results, and businesses have considerable discretion in selecting among recognized alternatives. *See generally* E. FARIS, ACCOUNTING FOR LAWYERS ch. 1 (3d ed. 1975); C. NICKERSON, ACCOUNTING HANDBOOK FOR NONACCOUNTANTS 1-13 (1986).

Illustrative of the uncertainty was the debate over Texaco's ability to satisfy the $12 billion Pennzoil judgment out of unencumbered assets. *See infra* note 62. Of course, the larger and more multifaceted the enterprise, the greater the subjectivity and uncertainty involved in answering questions of financial worth, capacity, and condition. It is this difficulty that leads us to believe that, in applying the good faith doctrine to large company filings, the courts consider factors other than the extent of the debtor's financial woes. *See infra* notes 189-93 and accompanying text.

54 According to the court, that Manville's economic pressures were "tort-related," and not the product of more prosaic forms of financial exigency, did not demonstrate a misuse of bankruptcy jurisdiction. *Johns-Manville*, 36 Bankr. at 740-41. The court correctly arrived at this conclusion based on the fact that under the Code, unlike the earlier Act, tort claims are fully dischargeable. 11 U.S.C. § 1141(d) (1988). *But see* Note, *Mass Tort Claims and the Corporate Tortfeasor: Bankruptcy Reorganization and Legislative Compensation Versus the Common Law Tort System*, 61 TEX. L. REV. 1297 (1983) (suggesting the inappropriateness of bankruptcy reorganization as a means for responding to mass tort liability) [hereinafter Note, *Mass Tort Claims*].

defending individual state court lawsuits.[55] Moreover, because a likely outcome of the latter alternative might be to unfairly reward those creditors who beat the swiftest path to the courthouse at the expense of their equally deserving but less zealous counterparts, the Manville court was able to square the filing with the core bankruptcy policy of promoting equality of treatment among similarly positioned parties.[56]

Like the court in *Continental Airlines*, the *Manville* court stressed the extreme factual dissimilarity between the garden variety one-asset debtor case and the filing by a major publicly held corporation, equating only the former with the kind of abuse that, in the court's estimation, the implied good faith requirement was designed to control.[57] Although both courts fell short of actually saying so, at work in each case was an apparent disinclination to sift too carefully through what in any large business filing is likely to be an admixture of complex motivations for seeking bankruptcy protection, so long as the debtor appears to have at least a reasonable chance of formulating a confirmable plan of reorganization.

Possibly, the courts' emphasis on underlying economic exigency belies the real impetus behind the courts' decisions in these cases. After all, the threat of economic ruination in the typical one-asset debtor case is no less real than it was for Continental Airlines or Manville. However, if the outcome in the good faith cases is explicable less in terms of solicitude for the prejudicial impact the filing will have on creditor interests narrowly defined, and more in terms of concern that Chapter 11 not be used by entities lacking both the intent and ability to fashion a successful

[55] *Johns-Manville*, at 740. The court noted that a "principal goal" of the Reform Act was "open access" to the bankruptcy system and that it was particularly illogical to allow dismissal based on the debtor's lack of good faith in filing when, "as a result of the bankruptcy, the creditors who will own the company are one in the same with the entity which emerges from the bankruptcy." *Id.* at 735-36 (citing *In re* UNR Indus., 725 F.2d 1111 (7th Cir. 1984)).

[56] *Id.* at 740. Of course, this conclusion hinged on the determination that Manville had no ability to financially manage claims arising out of asbestos-related injuries. At the same time, however, the court emphasized the absence of an insolvency requirement for Chapter 11 relief. *Id.* at 732. Some observers proposed that Manville's solvency should be regarded as the operative fact insofar as the good faith determination was concerned. *See* Note, *The Manville Bankruptcy: Treating Mass Tort Claims in Chapter 11 Proceedings*, 96 HARV. L. REV. 1121, 1127-28 (1983) ("If the creditors succeed in showing that Manville is more likely than not to remain solvent for the foreseeable future, the reorganization petition should be dismissed as an attempted misuse of the bankruptcy power."); Note, Manville: *Good Faith Reorganization*, *supra* note 11, at 152 (reorganization is proper if Manville is financially unable to accommodate all asbestosis victims); *see also* Furness v. Lilienfield, 35 Bankr. 1006, 1009-11 (D. Md. 1983) (court strongly admonished that in permitting cases like *Continental Airlines* and *Johns-Manville* to proceed, the bankruptcy courts had not adhered closely enough to the principles of good faith).

[57] *Johns-Manville*, at 739. The court did recognize, however, that filings by non-sham entities might nevertheless be considered "abusive" because of the debtor's lack of any need for reorganization of debt. *Id.* at 738 (citing *In re* Nancant, Inc., 8 Bankr. 1005 (Bankr. D. Mass. 1981), discussed *infra* note 64).

reorganization,[58] then the very size and respectability of the companies involved in these second-category cases may have allayed the courts' apprehensions. Nonetheless, whether apparently solvent public companies should be permitted to take shelter in Chapter 11 to implement long-term business planning objectives remains the subject of heated popular and political debate, which each new major filing seems to resurrect afresh.[59]

---

[58] *See supra* notes 43, 44 & 70 and accompanying text; *see also In re* The Bible Speaks, 65 Bankr. 415, 419 (Bankr. D. Mass. 1986), wherein Judge Queenan extensively discussed lack of good faith as a basis for dismissal of a Chapter 11 case, distinguishing between good faith in a factual sense and good faith in a jurisdictional sense. According to Judge Queenan, the former focuses on the debtor's subjective motive and the latter on whether the debtor's situation objectively justifies a reorganization. In analyzing these components, the court allowed that a predominant motive to harass or delay could sustain a charge of bad faith in the factual sense. *Id.* at 422. Based on the absence of any statutory financial standards for Chapter 11 relief, however, the court concluded that an operating entity with real debts, employees, and assets that was beset by financial problems could not be prevented from reorganizing under Chapter 11 simply because resolution of a specific creditor's dispute was the primary purpose for the filing. *Id.* at 428-30. *But cf. In re* HBA East, Inc., 87 Bankr. 248, 261-62 (Bankr. E.D.N.Y. 1988) (criticizing *Bible Speaks* as placing too much emphasis on subjective intent), discussed *infra* note 69.

[59] While the Continental Airlines and Johns-Manville filings were the only two public company cases to trigger actual contests over the question of good faith and the proper usages of bankruptcy, the past decade has witnessed an unprecedented number of reorganization petition filings by public companies of considerable size and financial strength. Covering a broad range of major industry sectors, many of these filings have been precipitated by the desire to secure an objective through the bankruptcy process that, for practical or political reasons, could not be obtained through more traditional channels. *See generally* Kennedy, *supra* note 8, at 210-13; Kroll, *Strategic Bankruptcy*, 8 CAL. LAW. 50 (1988). In each such instance, the issue of whether bankruptcy should be a means for accomplishing the goal in question has fueled heated public debate.

Included among these cases are the filings by A.H. Robins Co., Inc.; White Motor Corp.; UNR Industries, Inc.; and Amatex Corp. Like Manville's, each of these filings grew out of the frustration, cost, and disruption of having to defend multiple product liability lawsuits against both present and as yet unidentified claimants. *See generally* Olick, *Chapter 11—A Dubious Solution to Massive Tort Law Liability*, 18 FORUM 361 (1983); Comment, *The Manville Corporation Bankruptcy: An Abuse of the Judicial Process*, 11 PEPPERDINE L. REV. 151 (1983); Note, *Tort Creditor Priority in the Secured Creditor System: Asbestos Times, the Worst of Times*, 36 STAN. L. REV. 1045 (1984); Daniels, *Attorneys for Plaintiffs Object to Robins Filing*, N.Y. Times, Aug. 23, 1985, at D5, col. 5 (attorney representing several tort plaintiffs stated that his firm intended to ask the court to deny Robins bankruptcy protection because it is financially healthy); Schwadel, *Robins Files for Protection of Chapter 11*, Wall St. J., Aug. 22, 1985, at 3, col. 1 (stating that Robins bankruptcy petition listed total assets of $466 million against total liabilities of $206 million, exclusive of a $615 million reserve to cover Dalkon Shield claims).

Like the earlier filing by its sister company, Continental Airlines, the Chapter 11 filing by Eastern Airlines, Inc. (Case Nos. 89 B 10448-49, Bankr. S.D.N.Y. 1989) was caused by labor difficulties and raised anew questions about the use of bankruptcy to adjust labor relations and achieve results not possible directly under federal labor law. *See, e.g.*, DeGeorge & Fins, *Advantage, Lorenzo*, BUS. WK., July 10, 1989, at 25; *Eastern Requests Bankrupt Status to Cut Strike Loss*, N.Y. Times, Mar. 10, 1989, at A1, col. 1 (describing the filing as "the centerpiece of a strategy to wear down . . . striking machinists and . . . pilots until they agree to return to work."). In reaction to Eastern's filing, Congress passed legislation (HR 1231) on March 15, 1989 which would have established a Presidential emergency board under the Railway Labor Act to investigate the strike against Eastern. A similar board had resolved labor disputes between the airlines and their employees before that

3. *The Litigation Tactic Case*—Cases fitting neither the first category nor the second are, by default, members of our third grouping: litigation tactic cases. These cases differ from the classic one-asset debtor pattern because they involve ongoing, legitimate business enterprises. They differ as well from cases of the *Manville* and *Continental Airlines* ilk in that the decision to pursue Chapter 11 relief is not influenced nearly to the same degree by broad considerations of strategic business planning. Instead, the debtor in a litigation tactic case most often files in direct response to pressures emanating from a discrete dispute in which the debtor is involved. The objective of the debtor in such a case is to make use of the procedural incidents of bankruptcy, such as the automatic stay, and thereby secure a tactical advantage in the conduct of a specific two-party dispute.[60]

The most notorious of the litigation tactic cases involve petitions filed with the evident intention to circumvent state law requirements regarding the posting of a supersedeas bond as a condition to appealing an adverse judgment. Texaco's much-publicized Chapter 11 filing in the wake of Pennzoil's nearly $12 billion judgment against it is certainly the

industry's deregulation. *Labor's Bankrupt Strategy*, Wall St. J., Mar. 10, 1989, at A16, col. 1. However, President Bush vetoed the legislation on November 21, 1989, contending that government intervention would hinder the bankruptcy process. *See* 1 Bankr. L. Rptr. (BNA) 522 (Nov. 30, 1989).

Another novel approach to bankruptcy, and an accompanying controversy, was created by the first major public utility filing under the Code. The Public Service Company of New Hampshire's filing, which could be traced to delays and troubles encountered by the company in obtaining licensing for its Seabrook nuclear reactor, was the first bankruptcy filing by a major utility since the Depression. Critics assailed the filing as an improper attempt to circumvent normal regulatory approvals and rate ceilings. *See PS New Hampshire Seeks to Sidestep State Lid on Rates*, Wall St. J., Apr. 29, 1988, at 2, col. 3. The company cited the failure of the state regulatory system and the politicization of the process as the reasons for the company's bankruptcy filing. *The Bankruptcy that Wasn't Supposed to Happen*, PUBLIC UTILITIES FORTNIGHTLY, June 9, 1988, at 122.

Public company filings involving other unsettled political and economic problems could be cited, such as the legacy of the 1980s leveraged buyout frenzy showcased by the bankruptcies of Allied Stores Corp., Federated Department Stores, and Drexel Burnham Lambert, *see infra* notes 214-215, but we believe we have made our point. Litigated decisions favoring the debtor in *Continental Airlines* and *Manville* have not resolved the public and highly political debate over the use of the bankruptcy process as an instrument of corporate strategy by large and sophisticated business enterprises. Thus, legitimate questions remain about the limits of the bankruptcy process. And, as we argue generally in Part III of this Article, much about the scope of bankruptcy policy can be learned by observing the courts' use of the good faith device in the decided case law. This information is valuable both in a descriptive sense and because of its powerful predictive capabilities.

60 A word of clarification may be in order. Most one-asset debtor cases also involve essentially a two-party dispute: the debtor versus the secured creditor about to foreclose on the debtor's only asset. Thus, several one-asset debtor cases refer to the two-party nature of the dispute as an identifying factor. *See, e.g., In re* HBA East, Inc., 87 Bankr. 248, 260 (Bankr. E.D.N.Y. 1988); *In re* Mildevco, 40 Bankr. 191, 194 (Bankr. S.D. Fla. 1984). For this reason, those cases might well be included in the litigation tactic category. We have not done so because the "single real-estate-asset-on-the-eve-of-foreclosure-filing" has occurred with sufficient frequency, as to at least its own law and lore, to earn it a category of its own.

most striking example of this type of situation.[61] While that filing triggered a flurry of public debate over the good faith issue,[62] the bankruptcy court was not required to decide the question since Texaco's petition was never formally challenged on bad faith grounds. Other courts have split on the permissibility of the appeal bond avoidance tactic, the differing results usually being explicable by reference to the debtor's success in convincing the court of both financial need and a genuine intention to reorganize if the state court judgment is affirmed.[63]

A wide variety of underlying transactions, circumstances or events giving rise to what is essentially a discrete dispute between the debtor and some third party account for the other cases encapsulated within the broad category of litigation tactic cases.[64] In our judgment, these cases include recent decisions in which the bankruptcy courts have struggled to sort out the status and priority afforded to governmental agencies seeking to enforce orders issued pursuant to state and federal environ-

---

61 Bankr. Nos. 87 B 20142-44 (Bankr. S.D.N.Y. 1987). For a review of the rich pre-bankruptcy history of this case in the state and federal courts, see generally Texaco Inc. v. Pennzoil Corp., 784 F.2d 1133 (2d Cir. 1986), *rev'd*, 481 U.S. 1 (1987). *See also* Mnookin & Wilson, *Rational Bargaining and Market Efficiency: Understanding* Pennzoil v. Texaco, 75 VA. L. REV. 295, 300-09 (1989).

62 *See, e.g., A Break in the Action, Texaco's Chapter 11 Buys Time—and Maybe More*, TIME, Apr. 27, 1987, at 52 (citing Pennzoil officials as indicating that they might challenge the bankruptcy petition); Glasgall, Thompson & Norman, *Chapter 11 for Texaco? It's Not Impossible*, BUS. WK., Dec. 9, 1985, at 36; *Texaco Plays Hardball With Pennzoil by Planning to Use Bankruptcy-Law Petition to Whittle Down Its Liability*, Wall St. J., Apr. 14, 1987, at 26, col. 1 (citing a Pennzoil spokesman's comment that "Texaco has unencumbered assets sufficient to meet every liability—including the $10.3 billion judgment."); *Bankruptcy Option, Texaco Files Petition for Chapter 11 as Talks With Pennzoil Collapse*, Wall St. J., Apr. 13, 1987, at 1, col. 6.

63 *See In re* Harvey, 101 Bankr. 250, 252 (Bankr. D. Nev. 1989) (dismissing petition based on debtor's failure to present evidence of unavoidable financial ruin resulting from being required to post a bond); *In re* Holm, 75 Bankr. 86 (Bankr. N.D. Cal. 1987) and authorities cited in *Holm*. *Holm* adopted the generally accepted view that a debtor may in good faith file a Chapter 11 petition to avoid posting an appeal bond only if the debtor faces severe disruption of its business if enforcement of the judgment is not stayed pending appeal. *Id.* at 87. *But see In re* Karum Group, Inc., 66 Bankr. 436, 438 (Bankr. W.D. Wash. 1986) (debtor's use of bankruptcy's automatic stay to avoid posting a supersedeas bond was bad faith even though the amount of the judgment in question far exceeded the debtor's assets).

Had a motion to dismiss been filed, the issue of good faith in connection with the Texaco filing might well have turned on what was a much-contested issue; *i.e.*, whether Texaco's net worth was sufficient to cover the Pennzoil judgment. *See generally* Transworld Airlines, Inc. v. Texaco, Inc. (*In re* Texaco Inc.), 92 Bankr. 38, 40 (S.D.N.Y. 1988). For further discussion of this issue, see *infra* text accompanying notes 217-41.

64 For example, a good faith challenge has successfully been raised in a reorganization case alleged to have been filed solely for the purpose of having an ongoing dispute over a local tax liability determined by the bankruptcy court. *In re* Nancant, Inc., 8 Bankr. 1005 (Bankr. D. Mass. 1981). Courts also have rejected as beyond the contemplation of the bankruptcy law petitions filed to avoid the imposition of contempt sanctions in state court. *See* Johnson v. Markunes (*In re* Markunes), 78 Bankr. 875 (Bankr. S.D. Ohio 1987); *In re* Winn, 43 Bankr. 25 (Bankr. M.D. Fla. 1984). Likewise, in *In re* EPCO Northeast, Inc., 118 Bankr. 267, 270 (Bankr. E.D. Pa. 1990), the bankruptcy court imposed sanctions under Bankruptcy Rule 9011 on counsel in a Chapter 11 case filed "solely to delay and complicate impending state court litigation and [an] arbitration proceeding."

mental laws. Though the courts have not framed this issue in the language of the good faith doctrine, it raises the same underlying question: does the use of bankruptcy process to avoid the burden of hazardous or toxic waste cleanup costs constitute bad faith?[65]

Most often, bad faith charges have been levied when an apparently solvent debtor is perceived to have commenced a Chapter 11 case with the intention of favorably influencing the disposition of a private civil

---

65 Much of the litigation regarding the policy conflicts between the bankruptcy and environmental laws has occurred in the context of the debtor's right, when faced with violations of state environmental laws, to abandon waste sites under 11 U.S.C. § 554(a) (1988). In Midlantic Nat'l Bank v. New Jersey Dep't of Envtl. Protection, 474 U.S. 494 (1986), the Supreme Court, in a five to four decision, held that a judicially created exception to the trustee's unqualified abandonment power was properly recognized when necessary to protect the public's health and safety. *Id.* at 507. The Court cautioned, however, that this exception to the abandonment power was a narrow one. *Id.* at 507 n.9. Several subsequent decisions have thus construed *Midlantic* as only restricting the trustee's abandonment power when the situation poses "imminent harm" to the public health and safety. *See, e.g.*, Borden, Inc. v. Wells-Fargo Bus. Credit (*In re* Smith-Douglass, Inc.), 856 F.2d 12 (4th Cir. 1988) (permitting the trustee unconditionally to abandon a fertilizer plant despite water contamination violations); White v. Coon (*In re* Purco, Inc.), 76 Bankr. 523 (Bankr. W.D. Pa. 1987) (adopting a five-factor test set forth in *In re* Franklin Signal Corp., 65 Bankr. 268, 272 (Bankr. D. Minn. 1986) for analyzing whether to permit abandonment of hazardous waste sites in violation of state law). *But see In re* Microfab, Inc., 105 Bankr. 161, 169 (Bankr. D. Mass. 1989) (*Midlantic* requires full compliance with environmental laws); *In re* Peerless Plating Co., 70 Bankr. 943, 947 (Bankr. E.D. Mich. 1987) (rejecting *Franklin* in favor of a more restrictive stance on abandonment of hazardous waste sites). Obviously, an alternate analysis might rest on the basic considerations at work in the good faith cases. A brief attempt to outline such an analysis is undertaken *infra* text accompanying notes 242-49.

Closely related to the abandonment problem is the question of who pays for the clean-up. In Ohio v. Kovacs, 469 U.S. 274 (1985), the Supreme Court held that a state court injunction directing clean-up of a hazardous waste site gave rise to a "claim" subject to the automatic stay and dischargeable in bankruptcy. *Id.* at 279-80. The *Kovacs* holding, however, was carefully limited by the Court to the specific facts of the case, which included the pre-petition appointment of a receiver to take possession of the waste disposal site. Where the debtor has not been deprived of control over the site and the ability to accomplish the clean-up, some courts have permitted the state to continue enforcement under the state police or regulatory power exception to the automatic stay. *See* Commonwealth Oil Ref. Co. v. United States Envtl. Protection Agency (*In re* Commonwealth Oil Ref. Co.), 805 F.2d 1175 (5th Cir. 1986); Penn Terra Ltd. v. Department of Envtl. Resources, 733 F.2d 267 (3d Cir. 1984); 11 U.S.C. § 362(b)(5) (1988). This narrow reading of *Kovacs* also has been used to support the view that the state's claim is an administrative expense not dischargeable in bankruptcy. Lancaster v. Tennessee (*In re* Wall Tube & Metal Prods. Co.), 831 F.2d 118 (6th Cir. 1987); *In re* Better Brite Plating, Inc., 105 Bankr. 912, 917 (Bankr. E.D. Wis. 1989) (cost of cleanup is an administrative expense and property cannot be abandoned where there are unencumbered assets in the estate to pay for cleanup); *In re* FCX, Inc., 96 Bankr. 49 (Bankr. E.D.N.C. 1988). *But cf. In re* Dant & Russell, Inc., 853 F.2d 700 (9th Cir. 1988) (court denied landlord of property contaminated by a bankrupt debtor of an administrative priority for cleanup costs). Regarding the dischargeability question, in United States v. Whizco., Inc., 841 F.2d 147 (6th Cir. 1988), the court narrowly interpreted *Kovacs* to mean that, to the extent the debtor could comply with a pre-petition mine reclamation order without spending money, his bankruptcy did not discharge his obligation to do so. However, in United States v. Chateaugay Corp. (*In re* Chateaugay Corp.), 112 Bankr. 513, 525 (S.D.N.Y. 1990), the district court refused to follow *Whizco*, reasoning that under *Kovacs* if the environmental agency has an option to convert its claim into a right to monetary payment by, for example, performing the cleanup itself, the obligation must be regarded as dischargeable.

contest.[66] Typically, these cases find the debtor using the unique protection of the federal bankruptcy forum to obtain leverage in a legal contest with another party. However, they also may include two-party disputes in the form of intra-corporate squabbles among co-owners of a business when one of the parties perceives an advantage to be obtained by placing the business in a bankruptcy proceeding.[67] Further, because the tactical

---

66 *See, e.g.*, Barclays-American/Business Credit, Inc. v. Radio WBHP, Inc. (*In re* Dixie Broadcasting, Inc.), 871 F.2d 1023 (11th Cir. 1989) (relief from stay granted based on bad faith filing by financially secure debtors seeking relief from contract to sell radio stations); Furness v. Lilienfield, 35 Bankr. 1006 (D. Md. 1983) (bankruptcy filed in attempt to forestall and possibly block federal court RICO trial); *In re* Ravick Corp., 106 Bankr. 834, 844-51 (Bankr. D.N.J. 1989) (reorganization petition filed as a litigating tactic in an essentially two-party dispute over real estate contracts properly resolvable in state court); Gaudio v. Stamford Color Photo, Inc. (*In re* Stamford Color Photo, Inc.), 105 Bankr. 204, 207-08 (Bankr. D. Conn. 1989) (bankruptcy filed to flaunt state court order making corporate debtor alter ego of its sole shareholder); *In re* Schlangen, 91 Bankr. 834, 837-38 (Bankr. N.D. Ill. 1988) (primary purpose for initiating case was to confer federal jurisdiction over dispute involving issues of state law); *In re* HBA East, Inc., 87 Bankr. 248 (Bankr. E.D.N.Y. 1988) (Chapter 11 petition filed to obtain a perceived advantage in ongoing state court litigation dismissed for want of good faith); *In re* Business Information Co., 81 Bankr. 382 (Bankr. W.D. Pa. 1988) (bankruptcy filed in anticipation of denial of motion for stay pending appeal in federal court suit involving Fair Labor Standards Act violations); *In re* Noco, Inc., 76 Bankr. 839 (Bankr. N.D. Fla. 1987) (use of reorganization process to avoid contractual burdens and to litigate non-bankruptcy issues amounts to bad faith); *In re* Talladega Steaks, Inc., 50 Bankr. 42 (Bankr. N.D. Ala. 1985) (motivation of solvent debtor was other than to seek reorganization of financially stressed business); *In re* Port Richey Serv. Co., 44 Bankr. 634 (Bankr. M.D. Fla. 1984) (bankruptcy filed to delay enforcement of state court order regarding removal of property).

For examples of cases in which dismissal of a Chapter 11 petition was denied even though the filing was motivated primarily by a third-party dispute, see *In re* Taylor, 103 Bankr. 511 (D.N.J. 1989); *In re* McStay, 82 Bankr. 763 (Bankr. E.D. Pa. 1988); *In re* Consulting Actuarial Partners, Ltd., 72 Bankr. 821 (Bankr. S.D.N.Y. 1987); *In re* The Bible Speaks, 65 Bankr. 415 (Bankr. D. Mass. 1986) (debtor demonstrated honest intention to reorganize); *In re* Alton Telegraph Printing Co., 14 Bankr. 238 (Bankr. S.D. Ill. 1981) (creditor's judgment threatened to vitiate debtor's existence).

67 In Stolrow v. Stolrow's, Inc. (*In re* Stolrow's, Inc.), 84 Bankr. 167 (Bankr. 9th Cir. 1988), for example, the debtors were affiliated corporations owned by three family members embroiled in a dispute over control. In response to the charge that the bankruptcy court lacked jurisdiction because the sole motivation for the petitions was to secure a tactical advantage in an internal dispute over corporate control, the appellate panel reasoned that since the debtors were capable of satisfying the statutory requirement of proposing a plan in good faith which preserved going concern value and jobs, the bankruptcy court's finding of good faith in filing would not be disturbed. *Id.* at 171-72. In reaching this conclusion, however, the panel did not suggest that the standard of good faith required to confirm a plan under § 1129(a)(3) is identical to the standard of good faith which is a prerequisite to filing a Chapter 11 petition. *See In re* Madison Hotel Assocs., 749 F.2d 410, 424-25 (7th Cir. 1984) (district court erred in failing to recognize the legal distinction between the good faith required as a prerequisite to filing and to confirming a plan). We agree strongly with this proposition since, as discussed *infra* Part III, we perceive the good faith filing requirement as serving a function very distinct from the plan confirmation standards. However, not all commentators recognize this distinction. *See Cohn, supra* note 11, at 133 (stating that no court has suggested that the standard of good faith shifts as the case proceeds).

Other cases involving internecine warfare among shareholders include: *In re* Bicoastal Corp., 109 Bankr. 467 (Bankr. M.D. Fla. 1989) (Chapter 11 filing challenged on the basis that debtor corporation filed its petition merely to frustrate the election of a new board of directors); Gaudio v.

advantages that might be derived from a bankruptcy filing do not accrue solely to debtors, good faith challenges may be raised on this basis in involuntary cases as well.[68]

To a significant degree, these cases can best be understood (and most easily distinguished from one another) by each court's view of Congress's intention regarding the permissible scope of Chapter 11 relief.[69] Nevertheless, in a large majority of the cases falling into this final category, the judicial attitude that has emerged is that so long as valid reasons for filing exist, it is irrelevant that the petition may actually be motivated by other circumstances and events.[70]

Stamford Color Photo, Inc. (*In re* Stamford Color Photo, Inc.), 105 Bankr. 204 (Bankr. D. Conn. 1989) (Chapter 11 filing by corporate debtor dismissed for bad faith where former sole shareholder fraudulently transferred shares to deprive ex-spouse of any interest in the value of the enterprise); *In re* Justus Hospitality Properties, Ltd., 86 Bankr. 261 (Bankr. M.D. Fla. 1988) (bad faith alleged by shareholder who had been removed from debtor's management by creditor); *In re* Golden Ocala Partnership, 50 Bankr. 552 (Bankr. M.D. Fla. 1985) (filing initiated to resolve controversy over ownership and control of a nondebtor corporation dismissed for lack of good faith). *See also* Note, *Corporate Receiverships and Chapter 11 Reorganizations*, 10 CARDOZO L. REV. 285 (1988).

68 *See, e.g.*, Baker v. Auger (*In re* Baker), 709 F.2d 1063, 1064-65 (6th Cir. 1983) (dismissing involuntary case filed for sole purpose of effecting assignment of nonassignable claim); *In re* Winn, 49 Bankr. 237 (M.D. Fla. 1985); *In re* Basin Elec. Power Coop. v. Midwest Processing Co., 47 Bankr. 903 (D.N.D. 1984), *aff'd*, 769 F.2d 483 (8th Cir. 1985), *cert. denied*, 474 U.S. 1083 (1986); *In re* Win-Sum Sports, Inc., 14 Bankr. 389 (Bankr. D. Conn. 1981); *cf.* Carteret Savs. Bank, F.A. v. Nastasi-White, Inc. (*In re* East-West Assocs.), 106 Bankr. 767 (S.D.N.Y. 1989) (involuntary case not dismissed for lack of good faith despite presence of some indicia of bad faith).

Section 303(i)(2) expressly makes bad faith in filing relevant in involuntary cases by authorizing the court to impose actual and punitive damages against the offending creditors. 11 U.S.C. § 303(i)(2) (1988). That provision only becomes applicable, however, upon dismissal of the case other than by consent of all the parties. Therefore, § 303(i)(2) arguably does not make the question of bad faith relevant until there has been a dismissal on some other basis, and § 303 does not itself explicitly require good faith as a condition for entitlement to involuntary relief. Nevertheless, as in voluntary filings, courts have implied the requirement of good faith to permit a debtor to contest an involuntary petition not assailable under any other statutory ground. Of course, if successful, the debtor should then also be able to recover damages based on § 303(i)(2), since there would seem to be no reason to interpret bad faith in that context differently from the threshold requirement. *See generally* Carolin Corp. v. Miller, 886 F.2d 693, 701 (4th Cir. 1989). *Cf. supra* note 67 (suggesting that the test of good faith under § 1129(a)(3) may differ).

69 In *In re* HBA East, Inc., 87 Bankr. 248, 259 (Bankr. E.D.N.Y. 1988), for example, the court emphasized Congress's use of the phrases "restructure a business's finances" and "business reorganization" in describing the purpose of Chapter 11. H.R. REP. No. 595, 95th Cong., 1st Sess. 220-21, *reprinted in* 1978 U.S. CODE CONG. & ADMIN. NEWS 5963, 6179-80. The absence of a self-sufficient business played an important role in the *HBA East* court's ultimate determination that the filing in that case, prompted by a business dispute between the operators of a boxing promotion enterprise, was inappropriate for bankruptcy. By contrast, in *In re* The Bible Speaks, 61 Bankr. 415, 424-26 (Bankr. D. Mass. 1986), the court focused more on Congress's concern over expanding early and open access to Chapter 11 relief to support its conclusion that the filing was proper even though the debtor's prime purpose was to resolve a third-party dispute. *Id.* at 429; *see also In re* Furness v. Lilienfield, 35 Bankr. 1006, 1009 (D. Md. 1983) ("Chapter 11 was designed to give those teetering on the verge of a fatal financial plummet an opportunity to reorganize on solid ground and try again, not to give profitable enterprises an opportunity to evade contractual or other liability.").

70 This attitude about when a case filed for tactical reasons will be subject to dismissal is very

C. Assessment of the Implied Good Faith Filing Requirement in the Case Law

Having canvassed the areas where an otherwise eligible debtor's entry into bankruptcy has been contested on bad faith grounds, a few general observations can be made. First, the courts and commentators who have had occasion to address the subject almost unanimously have recognized the bankruptcy court's authority to impose a good faith filing requirement[71] and, by nearly the same margin, have endorsed its application of such a requirement. The doctrine has not, however, been without its critics,[72] and the recent increase in the number of good faith

---

different from the attitude that most courts have adopted in addressing the same question in the one-asset debtor cases. With relatively few exceptions, the test applied to Chapter 11 petitions allegedly filed as a litigation tactic seems to be an objective one: whether the debtor's circumstances suggest immediate and irrevocable financial distress. *See In re* Taylor, 103 Bankr. 511 (D.N.J. 1989), and cases cited *supra* note 66. By contrast, in the one-asset debtor situation, the test for good faith attaches greater importance to evidence of subjective intent. *Cf. supra* note 43 (for further discussion of the relative weight accorded to objective and subjective bad faith in the one-asset debtor case scenario). In part, the explanation for this distinction is obvious. By definition, in the classic one-asset debtor scenario, the debtor is always on the verge of imminent financial collapse. Thus, the test of good faith in those cases is more often couched in language of abusive purpose rather than financial exigency. On the other hand, some cases do strive to define a more objective basis for concluding the filing was in bad faith by emphasizing the lack of any reasonable prospects for reorganization. It is this inconsistency from one category of case to another (and even within a category, for that matter) that leads us to conclude that the distinction is more rationally explained by one of the central points of this Article—that courts use good faith as an instrumentality to control the evolution of the bankruptcy process. If this is so, then the standard and meaning of good faith necessarily will shift to some degree depending on both the type of case and the particular facts of a case to which the doctrine is applied. *See infra* text accompanying notes 179-84.

71 *See In re* HBA East, Inc., 87 Bankr. 248, 258 (Bankr. E.D.N.Y. 1988) ("this implicit good faith Chapter 11 prerequisite has been consistently upheld by the courts") and authorities cited therein; *see also supra* note 11 for a listing of commentaries relating to the subject.

72 One commentator has expressed the view that "imposition of a good faith requirement appears contrary to the statute, illogical, and unworkable in its application." M. BIENENSTOCK, BANKRUPTCY REORGANIZATION 28 (1987). Bienenstock maintains that redeploying assets under Chapter 11 to maximize value and allocate losses "ratably to creditors of equal rank is beneficial and virtuous regardless of whether the debtor also has lines of business that are profitable and not in need of reorganization." *Id.* at xxxi. Coming from a practitioner whose firm does an extensive amount of debtor work, this view perhaps comes as no surprise.

Taking a somewhat different tack, another commentator has criticized the good faith doctrine as obscuring the focus on more germane questions such as the proper definition of adequate protection and the appropriate uses of bankruptcy. Note, *Good Faith Inquiries Under the Bankruptcy Code*, *supra* note 11. This author contends that secured creditors, concerned that they will not receive full value in bankruptcy, cloak this worry by attacking the debtor's motive in the form of a good faith challenge. *Id.* at 802. Thus, the argument goes, if secured creditors were afforded full compensation, they would be indifferent to the debtor's bankruptcy filing. *Id.* at 813-15. This view, predicated on an economic-based theory of bankruptcy, is discussed *infra* note 117. It ultimately fails as an adequate exposition of the issue because it presumes a single, fundamental bankruptcy purpose which, however appealing in theory, is belied by the reality of modern day bankruptcy. Thus, as we develop in Part III of this Article, far from obscuring the more germane question of the proper uses of bankruptcy, the good faith doctrine is the vehicle by which bankruptcy's purposes are determined at any given point in time.

challenges may account for what appears to be the willingness of some courts to reconsider the wisdom of imposing broad extra-statutory constraints on access to bankruptcy relief.[73]

Second, in spite of the widespread acceptance of a good faith filing prerequisite, the standards by which good faith is to be judged remain ill-defined and obscure. This is not to suggest that fixed and immutable definitions are always possible, or even desirable. There is, however, reason to speculate that the lack of consensus over the role of the good faith requirement has encouraged a tendency to confuse the analytical task of formulating appropriate standards with the empirical process of identifying the factors that have coalesced to account for the dismissal of actual Chapter 11 petitions on this ground. If the good faith filing requirement is to serve as the judicial "policing mechanism" for assuring that the rehabilitative provisions of the bankruptcy law have been invoked for a purpose consistent with the objectives of bankruptcy policy,[74] then particular attention must be paid to the normative question of what are the

---

[73] In *In re* Cook, 98 Bankr. 624, 626 (Bankr. D. Mass. 1989), Judge Queenan, who also wrote the opinion in *In re* The Bible Speaks, 65 Bankr. 415 (Bankr. D. Mass. 1986) (discussed *supra* notes 44 & 69) referred to what he termed "[t]he somewhat insidious growth of a good faith filing requirement." After noting that "[a]nalysis of eligibility requisites under the rubric of a good faith standard adds nothing," he concluded that "[w]hether imposing a good faith filing requirement or interpreting the statutory filing standards, a court must be careful not to arrogate to itself the functions of the legislature." *Id.*; *see also In re* Gulph Woods Corp., 84 Bankr. 961, 971 (Bankr. E.D. Pa. 1988) (expressing doubt that there is a requirement that a Chapter 11 petition be filed in good faith (citing *In re* Latimer, 82 Bankr. 354, 363-64 (Bankr. E.D. Pa. 1988))).

In his dissenting opinion in Carolin Corporation v. Miller, 886 F.2d 693, 707 (4th Cir. 1989), Judge Widener argued that the courts have been precipitous in adopting an implied good faith filing requirement without first fully establishing the existence of an interstice in the statutory scheme that needs to be filled in by judicial patchwork. Without completely rejecting the judicially created good faith filing requirement, Judge Widener suggested that Congress's failure to carry forward the Bankruptcy Act's explicit good faith filing requirement in corporate reorganizations, *see supra* note 10, at least places the issue in some doubt. *Id.* at 707-08.

[74] The court in Furness v. Lilienfield, 35 Bankr. 1006, 1011 (D. Md. 1983) suggested precisely such a role for the good faith filing doctrine in bankruptcy. The court then went on to criticize the Continental and Manville bankruptcy filings on the ground that Chapter 11 was designed for businesses teetering on the edge of fatal financial peril, not for companies seeking to evade contractual obligations or avoid burdensome litigation costs. *Id.* at 1009, 1011. Of course, this criticism implicitly assumes what are and what are not worthy purposes. In other words, it is entirely possible that *In re* Continental Airlines Corp., 38 Bankr. 67 (Bankr. S.D. Tex. 1984) and *In re* Johns-Manville Corp., 36 Bankr. 727 (Bankr. S.D.N.Y.), *appeal denied*, 42 Bankr. 651 (S.D.N.Y.), *reh'g denied*, 42 Bankr. 654 (S.D.N.Y. 1984) were wrongly decided. In light of the good faith decisions in those cases, however, it is equally plausible that bankruptcy practice has come to serve needs other than those related to imminent financial collapse. Our analysis of the good faith issue specifically rejects the notion of any fixed, immutable purpose of bankruptcy. Thus, while our approach duly credits the core or historic purpose of bankruptcy, it also admits of both other purposes and changing purposes. Accordingly, we agree with the notion in *Furness* that the "good faith" requirement controls access to bankruptcy relief based on policy considerations regarding the goals of the bankruptcy system. However, we expand the analysis to consider shifting and evolving objectives, recognizing the role of the good faith doctrine in regulating that evolution. *See infra* notes 147 & 163-66 and accompanying text.

legitimate purposes of bankruptcy. We strongly suspect that the occasional disorder in judicial reasoning in this area can be traced to a generalized failure to give adequate consideration to the relationship between the implied good faith requirement and the underlying purpose of the bankruptcy system.

Certainly nothing is inherently wrong with the notion that persons, individual or corporate, should conduct their affairs in an honest, forthright, and reasonable manner. In the abstract, good faith as a sort of minimum fairness expectation is scarcely prey to criticism for asking too much of persons seeking the affirmative protection of the bankruptcy court. To recognize these plain truths about the good faith notion, however, is not to validate automatically the imposition of such a requirement as a prerequisite to all bankruptcy filings. What is more, to adopt the requirement is to say nothing about its nature and limitations in any particular context because good faith as a disembodied, free-floating value or ideal has no real substance.[75]

Even those who oppose implying nonstatutory conditions on access to bankruptcy relief do not do so on the basis, moral or otherwise, that parties should be free to act in bad faith. Therefore, to phrase the issue as whether there should or should not be a good faith filing requirement is to miss the point. The task to which the good faith analysis is truly addressed is the more problematic, and to a certain degree the more political one of line-drawing. While some courts routinely decry examination of a debtor's subjective motivation for entering bankruptcy,[76] the deliberate use of a legal procedure to accomplish an improper, ulterior purpose seems to be a major target of the implied good faith filing requirement.[77] The alternative objective standard, which focuses on the debtor's ability to effectuate a successful reorganization, simply does not explain the cases either in terms of accounting for their existence or rationalizing their outcomes.

Arguably, if the only reason for creating and imposing a good faith test in Chapter 11 was to eliminate at the earliest juncture cases involving

---

[75] *See generally supra* note 43 and *infra* text accompanying notes 168-72 for further discussion of the "good faith" concept as a component in the vocabulary of the law.

[76] *See, e.g., In re* Taylor, 103 Bankr. 511, 520-21 (D.N.J. 1989) (bad faith would not be found where Chapter 11 petition was justified by debtor's financial condition, even though real motive for filing was to avoid specific contractual obligations); *In re* HBA East, Inc., 87 Bankr. 248, 261-62 (Bankr. E.D.N.Y. 1988) ("the standard is an objective one rather than a question of the subjective intention of the petitioners"); *In re* Johns-Manville Corp., 36 Bankr. 727, 736-37 (Bankr. S.D.N.Y.) (debtor's motivation to obtain relief from multiple health-related lawsuits did not establish bad faith where the debtor's objective financial circumstances presented a pressing need for economic reorganization), *appeal denied,* 42 Bankr. 651 (S.D.N.Y.), *reh'g denied,* 42 Bankr. 654 (S.D.N.Y. 1984).

[77] This is the view of good faith that Ordin advances in support of an implicit good faith prerequisite to the filing or continuation of a proceeding under Chapter 11. Ordin, *supra* note 11, at 1796-97; *see also supra* note 58 and accompanying text for citation of additional authority discussing this and related views on the object of the good faith inquiry.

companies with no prospect for successful reorganization, there would have been no pressing need to go beyond the four corners of the Code. Section 1112(b) provides ample statutory authority for dismissing a case when there is no realistic hope for reorganization.[78] While a motion to dismiss on that ground may be premature until the debtor-in-possession has had some opportunity to explore its options for rehabilitation, nothing in the language or structure of the statutory scheme would preclude a more pre-emptory application of section 1112(b) in an obvious case.[79] Likewise, by supplying the court with authority to furnish a mortgagee with relief from the automatic stay, section 362(d) of the Code affords an effective remedy for secured creditors in the one-asset debtor filing designed solely to buy time and avoid an imminent mortgage foreclosure.[80]

Therefore, the most compelling and convincing explanation of a separate, implied good faith filing barrier is not the one that concerns itself with the need for a procedural mechanism to abort the patently hopeless case straightaway. Rather, it is the one founded on the desirability of

---

[78] *See* 11 U.S.C. § 1112(b)(1)-(3) (1988); *In re* Park Place Assocs., 118 Bankr. 613 (Bankr. N.D. Ill. 1990). This is essentially the point raised by Judge Widener in his dissent in Carolin Corporation v. Miller, 886 F.2d 693, 707 (4th Cir. 1989). Additionally, dismissal pursuant to § 1112(b) may be initiated by the court sua sponte. *See* S. REP. NO. 989, 95th Cong., 2d Sess. 117, *reprinted in* 1978 U.S. CODE & ADMIN. NEWS 5787, 5903; *see also* 11 U.S.C. § 105(a) (1988), which was amended by § 203 of the Bankruptcy Judges, United States Trustees, and Family Farmer Bankruptcy Act of 1986, Pub. L. No. 99-554, 100 Stat. 3088, to provide that "[n]o provision of this title providing for the raising of an issue by a party in interest shall be construed to preclude the court from, sua sponte, taking any action or making any determination necessary or appropriate to enforce or implement court orders or rules, or to prevent an abuse of process." *See also supra* note 16.

[79] *See* H. REP. NO. 595, 95th Cong., 1st Sess. 405, *reprinted in* 1978 U.S CODE CONG. & ADMIN. NEWS 5963, 6361, which provides that "[s]ubsection (b) gives wide discretion to the court to make an appropriate disposition of the case when a party in interest requests. . . . [c]ause may include the inability to effectuate a plan . . . ." The only limitation, therefore, on the court's ability to dismiss for cause under § 1112(b) is the requirement of notice and a hearing; however, that requirement would not seem to impose any serious impediment, *see* 11 U.S.C. § 102(1) (1988), and would probably be required in connection with any motion to dismiss, whether brought pursuant to § 1112(b) or otherwise.

[80] This point is made by both M. BIENENSTOCK, *supra* note 72, at 31, and Cohn, *supra* note 11, at 137-39; *see also* Barclays-American/Business Credit, Inc. v. Radio WBHP, Inc. (*In re* Dixie Broadcasting, Inc.), 871 F.2d 1023, 1026 (11th Cir. 1989) (petition filed in bad faith justifies relief from the stay), and authorities cited *supra* note 15.

There is some question, however, whether § 362(d)(2), which provides for relief from stay where the debtor has no equity in the property, and the property is not necessary to an effective reorganization, would be responsive to an improperly motivated filing where the debtor possesses equity in the property comprising its major asset. *See* Phoenix Picadilly, Ltd. v. Life Ins. Co. of Va. (*In re* Phoenix Picadilly, Ltd.), 849 F.2d 1393, 1394-95 (11th Cir. 1988) (debtor's equity in property is not dispositive of the good faith issue); *see also supra* note 32. In such a case, the secured creditor typically would also be denied relief under § 362(d)(1) since, absent other risk factors, its interest in the property would be considered adequately protected by the equity cushion. *See, e.g.*, Pistole v. Mellor (*In re* Mellor), 734 F.2d 1396 (9th Cir. 1984). Thus, engrafting a good faith component onto the "for cause" language in § 362(d)(1), or providing alternative relief through an implicit good faith filing requirement, could be justified as necessary to deal with this circumstance.

forestalling the filing aimed at achieving an objective that, in light of prevailing legal and societal norms, is beyond the accepted purposes of the bankruptcy process. Thus rationalized, the good faith filing requirement is a dynamic one. Confusion over this point holds the potential to create enormous mischief. For example, if the articulated standard is the ability to carry the proceeding to a successful conclusion, then the implicit good faith filing requirement will never stand in the way of Chapter 11 filings by large, resource-rich business enterprises. On the other hand, if the requirement is perceived as protecting the integrity of the process, then each case will stand or fall on the basis of whether or not its continuance would compromise the purposes of bankruptcy, an inquiry which might be influenced, but which is not controlled, by the size of the debtor.

This approach necessarily implicates the more fundamental question of the purposes of the bankruptcy system. In what has risen nearly to the level of a solemn utterance, it is customary to list the two major objectives of bankruptcy law as: (1) providing debtors with a financial fresh start; and (2) providing creditors with an orderly procedure for repayment of their claims. As bankruptcy emerges from the well-defined niche which it occupied for so many decades, however, it is becoming increasingly clear that these aphoristic and colorless justifications are not enough. Heightened awareness of the multitude of areas where bankruptcy process can be used to accomplish specific goals and objectives has resulted in an expanded array of motivations which can influence a particular debtor to consider bankruptcy as a realistic alternative to other courses of action. Bankruptcy is no longer reserved for the seriously or terminally ill debtor, and it no longer operates on the periphery of commercial law and practice. Consequently, the potential for collision between bankruptcy policy, however defined, and the policies underlying other substantive areas of law is growing.[81] In a halting and uncertain way, the good faith filing requirement has been directed at ironing out these policy conflicts in individual cases. Greater understanding of that

[81] Dean Thomas Jackson, and others writing from an economics-based theory of bankruptcy, vehemently reject the notion of conflict between bankruptcy policy and the policies underlying other areas of the law. *See* T. JACKSON, THE LOGIC AND LIMITS OF BANKRUPTCY LAW 21-27 (1986); Baird, *Loss Distribution, Forum Shopping and Bankruptcy: A Reply to Warren*, 54 U. CHI. L. REV. 815, 824-28 (1987). They do so primarily on the basis of their fundamental belief that, to most effectively serve its sole function of maximizing asset values, bankruptcy should have no substantive policy agenda of its own, and instead should mirror the relative entitlement scheme of state law to the greatest extent possible. These views are discussed in more depth *infra* notes 82-117 and accompanying text. As a descriptive matter, however, bankruptcy has become a vehicle to which business interests have resorted to accomplish strategic and tactical objectives not obtainable under state law. Often this entails allocating and deploying assets in a manner contrary to or inconsistent with state law rights and priorities. *See generally* Kennedy, *supra* note 8, at 214 (bankruptcy still provides the best forum for resolving conflicting claims in cases where a multitude of interests may be legitimately entitled to protection). Recognition of this expanded role of bankruptcy, whether defensible or not on theoretical grounds, is the catalyst for our reconsideration of the use and function of the judicially implied good faith filing requirement.

fact would, we believe, lead to more thoughtful application of the requirement. In addition, it would significantly enhance discussion on the nature and scope of the good faith filing requirement.

II. BANKRUPTCY THEORY AND THE GOOD FAITH FILING IMPERATIVE

A. *Collectivist and Traditional Theories*

We have indicated that the threshold good faith requirement can be analyzed only with reference to its efficacy in advancing the underlying goals and objectives of the bankruptcy process. It would be impossible to meaningfully entertain questions about the rightful province of bankruptcy without a clear idea of the purpose of the bankruptcy process. It seems odd, but early scholarship neglected to develop a literature from which discussion of bankruptcy's objectives might proceed, leaving it to recent scholars to explore such fundamental policy questions.[82] In any event, two schools of thought have lately emerged. One view we refer to here as Collectivism,[83] in honor of its central premise that the single end purpose of bankruptcy is or should be efficient debt collection.[84] The

---

82 Dean Jackson oberved, "Neither *Report of the Commission on Bankruptcy Laws of the United States* . . . ('A Philosophical Basis for a Federal Bankruptcy Act') nor Shuckman, *An Attempt at a 'Philosophy of Bankruptcy'* . . . provides a cohesive normative approach that can be used with precision to examine the rights of creditors *inter se*," notwithstanding the highly suggestive titles of those efforts. Jackson, *supra* note 6, at 858 n.6. In an article in which she debates Baird on the matter of the underlying policies of bankruptcy, Warren notes: "Currently, the policies endorsed to support bankruptcy pronouncements are wide-ranging and, at the extremes, very much in opposition. Despite the critical importance of different policy presumptions, the policy elements underlying most discourses are asserted only obliquely, and they are rarely challenged directly." Warren, *Bankruptcy Policy*, 54 U. CHI. L. REV. 775, 776 (1987) (footnote omitted).

Of course, bankruptcy only recently has become a "booming business" and the subject of heightened attention among academics. *Id.* at 775. Bankruptcy assumed a high profile in the 1980s, when it became "more visible . . . more controversial and its perceived usefulness more widespread." T. JACKSON, *supra* note 81, at 1. Recent scholarship reflects the accuracy of these sentiments. *See, e.g.*, Cuevas, *Due Process and Bankruptcy Code Section 1102: The Concept of Adequate Representation in Large and Mega Reorganizations*, 94 COM. L.J. 314 (1989) (suggesting that new-era "mega-reorganizations" like those undertaken by Johns-Manville, Texaco, Continental Airlines, and A.H. Robins pose new questions about the adequacy of representation of multifarious interests implicated in massive reorganizations); Kennedy, *supra* note 8 (discussing the bankruptcies of Johns-Manville, Kovacs, and Quanta Resources, all new-era cases).

83 This is a term borrowed from Warren, *supra* note 82, and is, we believe, generally descriptive insofar as it makes clear that Collectivism holds debt-collectivizing to be the central concern of bankruptcy. Any suggestion inherent in the word "Collectivism" of a political bent should be revised out of the reader's understanding of the term as, perhaps, ironic.

84 The chief advocates of this premise have been Professor Douglas G. Baird and Dean Jackson. *See, e.g.*, Baird & Jackson, *supra* note 6. That bankruptcy should function in business bankruptcies solely as a debt collection device is one of Jackson's first principles of bankruptcy. *See* T. JACKSON, *supra* note 81, at 5. *But see infra* notes 124-25 and accompanying text (discussing recent criticism of the idea that debt collection alone is, or should be, the purpose of bankruptcy). Some scholars otherwise generally in sympathy with the Collectivists as to the importance of the debt collectivizing function seem reluctant to proclaim it the only function of bankruptcy. Professor Scott, for instance,

second school of thought we refer to as the Traditional view,[85] although, strictly speaking, it does not present a system of bankruptcy in the sense that Collectivism does.

"Collectivism," as we use that term, should be taken to mean the set of shared fundamental assumptions and postulates of a group of scholars writing mainly from an economics-based perspective of the law.[86] While a number of scholars have contributed to the formulation of the Collectivist view, Collectivism rises to the status of a unified theory mainly in the hands of Professor Baird and Dean Jackson.[87] For the sake of convenience we speak of Collectivism as the single product of their collaborative work, while here and there calling attention to their individual efforts.[88]

For the Collectivists, as noted above, bankruptcy serves a single pur-

---

has been a contributor to the discourse on bankruptcy as a collective regime. *See, e.g.*, Jackson & Scott, *On the Nature of Bankruptcy, supra* note 6; Scott, *Through Bankruptcy with the Creditors' Bargain Heuristic*, 53 U. CHI. L. REV. 690 (1986). However, Scott reintroduces the "fresh start" objective back into business bankruptcies involving small scale corporate debtors. *See* Scott, *Sharing the Risks of Bankruptcy:* Timbers, Ahlers, *and Beyond*, 1989 COLUM. BUS. L. REV. 183, 189 (1989).

85 Like the term "Collectivism", this term is borrowed from the Warren-Baird debate. *See* Baird, *supra* note 81, at 816.

86 In addition to Baird and Jackson, we certainly would include Theodore Eisenberg and Alan Schwartz among the prominent scholars writing in the tradition of finance theory. *See, e.g.*, Eisenberg, *Bankruptcy Law in Perspective*, 28 UCLA L. REV. 953 (1981); Schwartz, *Security Interests and Bankruptcy Priorities: A Review of Current Theories*, 10 J. LEGAL STUD. 1 (1981). More lately, Professor Scott has also joined the fray. *E.g.*, Jackson & Scott, *On the Nature of Bankruptcy, supra* note 6.

To be sure, the finance theory tradition in this area is not without its critics. *See, e.g.*, Kripke, *Law and Economics: Measuring the Economic Efficiency of Commercial Law in a Vacuum of Fact*, 133 U. PA. L. REV. 929 (1985); Shupack, *Solving the Puzzle of Secured Transactions*, 41 RUTGERS L. REV. 1067 (1989). Jackson and Schwartz respond to Kripke in *Vacuum of Fact on Vacuous Theory: A Reply to Professor Kripke*, 133 U. PA. L. REV. 987 (1985).

87 Examples of their individual efforts include: Baird, *Environmental Regulation, Bankruptcy Law, and the Problem of Limited Liability*, 18 ENVTL. L. REP. 10352 (1988); Baird, *A World Without Bankruptcy*, 50 LAW & CONTEMP. PROBS. 173 (1987); Baird, *The Uneasy Case for Corporate Reorganization*, 15 J. LEGAL STUD. 127 (1986); Jackson, *Translating Assets and Liabilities to the Bankruptcy Forum*, 14 J. LEGAL STUD. 73 (1985); Jackson, *Avoiding Powers in Bankruptcy*, 36 STAN. L. REV. 725 (1984); Jackson, *supra* note 6. Collaborative work includes: Baird & Jackson, *Bargaining After the Fall and the Contours of the Absolute Priority Rule (In Honor of Walter J. Blum)*, 55 U. CHI. L. REV. 738 (1988); Baird & Jackson, *supra* note 6; and the jointly authored text, D. BAIRD & T. JACKSON, CASES, PROBLEMS, AND MATERIALS ON BANKRUPTCY (2d ed. 1990). We do not here dismiss the importance of individual contributions; rather, we simply take cognizance of substantial agreement on fundamental assumptions about bankruptcy policy.

88 *E.g.*, Jackson is primarily responsible for developing the hypothetical bargain model. *See supra* note 6. Different aspects of Collectivist thought also receive varying emphasis. Baird, for instance, frequently speaks of the forum shopping that may follow from redistribution in bankruptcy. *See, e.g.*, Baird, *supra* note 81. Jackson, in his individual works, seems more inclined to speak of the negative effects of redistribution in terms of the resulting inefficient deployment of assets. *See, e.g.*, Jackson, *supra* note 6, at 860. In either case, the central assertion is the same—that bankruptcy should leave state law distribution schedules largely undisturbed. *See generally infra* notes 107-08 and accompanying text.

pose: it is a federal debt collection system.[89] Accordingly, bankruptcy is properly invoked only in response to a common pool problem,[90] a term Jackson uses to describe the situation created when a debtor's assets are insufficient to satisfy the demands of a common pool of claimants.[91] The purpose of bankruptcy—or, to use Jackson's term, the "first principle" of bankruptcy[92]—is to serve as a debt collection device targeted to the common pool problem.[93]

Bankruptcy, of course, does not have a monopoly over the business of debt collection. It is an alternative to state law schemes,[94] the main features of which are a set of creditor entitlements and a system of distribution priorities based upon the results of a race among creditors.[95] Thus it is that under state law an individual creditor is moved to pursue its collection remedies with alacrity while something remains of the

---

[89] *See, e.g.*, Baird & Jackson, *supra* note 6, at 103. Putting aside the principle of a fresh start for the business debtor, *but see* Scott, *supra* note 84, Jackson views bankruptcy as a collection device aimed at asset deployment: "The question of how assets are used is the focus of the other principal role of bankruptcy law .... This role ... is that of bankruptcy as a collective debt-collection device, and it deals with the rights of creditors . . . *inter se*." T. JACKSON, *supra* note 81, at 5; *see also* Jackson, *supra* note 6, at 857.

[90] *See infra* note 93.

[91] Jackson portrays creditors hoping to maximize recovery on their individual claims from a debtor's limited assets as similar to mineral interest owners with drilling rights in the same oil reservoir. In the latter situation, each owner will act to maximize production from its wells before the recovery efforts of its fellows deplete the resource, notwithstanding deleterious effects on future production from the structure. A slower rate of production, enforced by statutory unitization, assures maximum recovery of the resource for the collective benefit of the interest owners. Jackson sustains the metaphor in comparing the bankruptcy process to statutory unitization. *See* Jackson, *supra* note 6, at 864 n.34.

[92] "In analyzing bankruptcy law ... it helps to start by identifying first principles." T. JACKSON, *supra* note 81, at 2.

[93] Jackson tells us that "bankruptcy appropriately responds when multiple claimants are likely to exercise individual creditor remedies and the debtor does not have enough assets to satisfy them." *Id.* at 197. Thus, "one wants to demark cases where there is likely to be a common pool problem and ... exclude [from bankruptcy] those cases that are likely to be fueled simply by a selfish claimant seeking a strategic advantage." *Id.* at 199; *see also id.* at 193-94 (discussion of *In re* Tinte Constr. Co., 29 Bankr. 917 (Bankr. E.D. Wis. 1983)).

[94] "Indeed, Bankruptcy law is an ancillary, parallel system of debt collection law." T. JACKSON, *supra* note 81, at 4. Warren, whom we have appointed spokesperson of the Traditional view (admittedly without having consulted her on the matter) based on her debate with Baird, *see supra* note 82, agrees that bankruptcy is an alternate system of collection. She rejects, however, the idea that it is or should be an alternate system and nothing more: "The current debt collection system [comprised of state law collection schemes and the law of bankruptcy] treats these issues in different fora: state collection laws cope with a wide spectrum of limited defaults, while the bankruptcy scheme concentrates on default in the context of the debtor's imminent collapse." Warren, *supra* note 82, at 782. Thus, while Warren regards bankruptcy as an alternate debt collection scheme, it is one capable of embracing a host of complex problems created in the wake of enterprise failure in an integrated economic system. *Id.* at 783. *But see* Baird & Jackson, *supra* note 6, at 102-03.

[95] *See, e.g.*, U.C.C. § 9-301(1)(b) (lien creditor is prior to a secured creditor provided the lien creditor acquired its lien before the secured party perfects); U.C.C. § 9-312(5) (priority among conflicting security interests based on time of filing or perfection); OKLA. STAT. tit. 12, § 737 (1989) ("In all . . . cases, the writ of execution first delivered to the officer shall be first satisfied.").

debtor's assets. Those who arrive early to the repast are most likely to be fully satisfied, perhaps leaving little or nothing to succor the tardy. Some are satiated while others starve.

If anything is to be condemned in the scramble for assets[96] that distinguishes state law debt collection, it is perhaps that the resultant, piecemeal dismemberment and sale of a debtor's assets[97] are not well calculated to bring the highest price for those assets. Further, whatever value is realized is unlikely to be distributed proportionately among creditors. In contrast, were the integrity of the assets preserved, either to be disposed of in an orderly way or left with the debtor in an attempt to rehabilitate its faltering enterprise, they would enjoy a greater value, such that it could be said that they were more efficiently and, incidentally, more equitably deployed.[98] Naturally, the enhanced aggregate value of the debtor's assets from more efficient deployment would inure finally to the group of common claimants qua common pool. If resolution of the common pool problem through efficient asset deployment is our goal, then state law debt collection schemes fail us in this critical particular.[99]

What if instead of a system that engenders a snarling pack of creditors all at cross purposes, we envision a system wherein creditors agree among themselves to act for the common good of the pool *in advance* of a common pool problem; that is, a system in which creditors bargain in

---

96 The mad dash to collect precipitated by state law first-in-time schemes is colorfully described in D. BAIRD & T. JACKSON, TEACHER'S MANUAL: CASES, PROBLEMS, AND MATERIALS ON BANKRUPTCY 12-13 (1st ed. 1985) as a helter-skelter car race.

97 This is the consequence of multiple individual creditor lawsuits and attempts to satisfy judgments through state law execution and levy.

98 The value of assets sold piecemeal pursuant to foreclosure is customarily referred to as liquidation value. Liquidation value is what the asset will bring at forced sale less the costs of disposition. Liquidation value, in other words, assumes an asset in the hands of a debtor enterprise without a future.

In contrast, going concern value assumes a viable enterprise. The going concern value of a firm's equipment is measured by reference to the contribution of the equipment to continuing enterprise revenue in the present and *in futuro*. Where the assets to be valued are inventory, their going concern value would include mark-up. Generally speaking, going concern values exceed liquidation values. Inventory in the hands of a going concern, therefore, would fetch a higher price than inventory sold piecemeal upon foreclosure by a liquidation. Similarly, equipment will usually have a greater going concern value than liquidation value. Fortang & Meyer, *Valuation in Bankruptcy*, 32 UCLA L. REV. 1061, 1063-65 (1985).

For a brief discussion of going concern versus liquidation value in the context of Collectivism, see, Jackson & Scott, *supra* note 6, at 159.

99 Bankruptcy law and state collection law are both systems of debt collection, and, as such, are alternative schemes for that purpose. On the other hand, Warren has argued convincingly that the focus of the two systems is quite different so that there is by no means a complete coincidence of purpose: "A central purpose of state debt collection law is to provide a means for collection of a single unpaid debt. State collection law swings into action on the complaint of a single creditor, and it provides that creditor an avenue to pursue payment of the obligation owed to it." Warren, *supra* note 82, at 782. Thus, it is hardly surprising that state collection law is ill suited to the common pool problem, since it "does not address the possible consequence that the collection will render the debtor unable to pay its remaining creditors." *Id.*; *see also supra* note 94.

advance of financial reversals that would place them in competition for the debtor's limited assets? Would creditors ever agree voluntarily to act for the common pool at the cost of forfeiting their state law right to seek full recovery, even acknowledging that full recovery might depend on winning the race to judgment? Might creditors be coaxed out of their singular, all-consuming impulse to seek full recovery *at the expense* of the common pool if necessary?[100]

It would, of course, be foolishness to suppose creditors would bargain altruistically. Jackson postulates, however, that were creditors able to bargain *ex ante*, their own selfish impulses would supply the energy to impel and sustain an agreement that would yield an efficient deployment of a debtor's assets. Specifically, Jackson asserts that a creditor's interest in avoiding monitoring costs[101] and collection costs,[102] and in averting the risk of collecting nothing under state law[103] would motivate a credi-

---

100 If self-serving, such behavior is undeniably rational. We may, for the sake of convenience, come to regard a homogeneous group of creditors collectively, but we can hardly expect the emergence of a group mind as a result. Individual creditors can be relied upon to pursue their individual interests without regard for the impact upon the total recovery for the common pool. This phenomenon, referred to in game theory as the "prisoner's dilemma," arises "whenever certain rules are in the interests of an entire class of persons, but, because of an inability to reach a collective solution, each class member acts out of immediate self interest in such a way that a less efficient solution results." Jackson, *supra* note 6, at 862.

101 Monitoring costs, or "strategic costs" as Jackson calls them, *see id.* at 861, are incurred in self-defense by creditors against the chance they might arrive at the courthouse only after their fellows have long since denuded the debtor of its assets. Just how much it costs to monitor a debtor or actions against it by competing creditors is difficult to say. Surely, monitoring costs must vary according to how well equipped the creditor is to monitor at low cost and according to the nature of the creditor's relationship to the debtor. For instance, a close working relationship and intimate knowledge of a debtor-firm's internal affairs might reduce the need for external monitoring. It is difficult to imagine, however, that monitoring ever would be costless for most creditors. In discussing monitoring costs and the role they may play in explaining the nature and existence of secured creditors, Dean Jackson and Professor Kronman have suggested that monitoring may be easier and cheaper for some business creditors than others. Jackson & Kronman, *Secured Financing and Priorities Among Creditors*, 88 YALE L.J. 1143, 1155-60 (1979).

In any event, the proposition is that monitoring costs can be eliminated by eliminating the need to monitor. The need to monitor, in turn, can be eliminated through a bargain wherein every common pool member relinquishes the right to pursue full recovery under state law in exchange for the certain knowledge of a lesser recovery. The value of the diminished recovery is increased by the savings in monitoring costs, making the bargain all the more attractive. *See* Jackson, *supra* note 6, at 861-62.

102 "A single inquiry into recurring collection questions is likely to be less expensive than the multiple inquiries necessary in an individualistic remedies system." *Id.* at 866.

103 That is, risk-averse creditors would presumably forego the possibility of higher recovery under the state law regime for a lesser but certain recovery under a collectivising agreement among creditors. *See* T. JACKSON, *supra* note 81, at 15. In our own experience, however, creditors often prove arrogant in assessing their ability (or that of their lawyers) to anticipate eventualities and act against a debtor's assets with sufficient alacrity to ensure full recovery. Moreover, it would seem that some creditors actually are better postured than others to monitor a debtor for signs of difficulty. Professor Carlson has observed:

Historic creditors differ in their leverage and knowledge, their skill in obtaining payment or tor to bargain away the high risk prospect of full recovery based on state law entitlements. Thus relieved of the counter-productive incentives engendered by state law grab-bag collection remedies, the constituents of the common pool could act in concert for the most efficient deployment of assets, an enlarged aggregate recovery,[104] and, incidentally, enhanced individual recovery (though, of course, less than full recovery).

The fact is, however, that the creditors' bargain is destined to exist only in hypothesis because circumstances are unlikely to align themselves in a fashion to offer an occasion for the bargain to occur in reality.[105] What is required, therefore, is an edict, rather than an invitation, to "bar-

---

> liens, and their opportunity costs of litigating. Profit maximizing creditors who are powerful vis a vis other creditors would not agree to give up power to weaklings unless they were compensated for it. Creditors who are weak would love to take power from stronger creditors if they could.

Carlson, *Philosophy in Bankruptcy*, 85 MICH. L. REV. 1341, 1349 (1987). *But see* Jackson, *supra* note 6, at 863-64.

104 This assumes piecemeal disposition of the debtor's assets from a succession of individual creditor actions under state law. The statement further assumes that going concern value exceeds liquidation value. Jackson, *supra* note 6, at 864. For a brief discussion of liquidation and going-concern values, see *supra* note 98.

105 Jackson attributes the unlikelihood of the *ex ante* bargain in reality to the constant change in membership of the creditor pool over the life of the debtor enterprise. Since the group of creditors is not static, not even the debtor could identify and assemble the bargainers at the outset. Jackson, *supra* note 6, at 866 n.44.

Were matters otherwise ordered (*i.e.*, if a static pool of unsecured claimants could be identified and assembled *ex ante*), there is reason to believe there would yet be significant absences within the assemblage—namely, property claimants. Most representative of claimants within this class is the Article 9 secured creditor, whose participation in the bargain is acknowledged to be a matter of some moment, *see id.* at 869, for two reasons. First, secured creditors are likely to charge the administrative costs of foreclosure and sale back to the collateral pursuant to § 9-504(1), reducing the surplus (equity) that otherwise would be available to the common pool if the secured creditor were oversecured, and resulting in an increased claim against the debtor's remaining assets. The common pool of claimants would certainly benefit were the secured party to bargain away its repossession and foreclosure rights *ex ante*, eliminating the prospect of additional demands upon assets in the form of collection expenses.

Second, should the secured creditor participate in the *ex ante* bargain and agree to forego its rights of repossession and sale, the collateral would remain available to the debtor enterprise. Where the collateral would enjoy a greater going concern value than liquidation value, *see generally supra* note 98, its continued availability would redound to the benefit of the common pool. *See* Jackson, *supra* note 6, at 868.

What might induce fully secured creditors, whose recovery is assured in any event, to bargain for the benefit of the common pool of unsecured claimants? Frankly, unless the common pool of claimants were willing to share the resultant increase in their recovery, *see, e.g.*, *id.* at 869, there would be no inducement at all. *See id.* at 870 n.62. As one reviewer has observed, Jackson never tells us why a secured creditor would become party to such a bargain. *See* Warner, Book Review, 20 URB. LAW. 489 n.3 (1988) (reviewing T. JACKSON, *supra* note 81). The inducement of payment out of the enlarged recovery of the common pool is, of course, as hypothetical as the *ex ante* bargain itself. The most we learn from Jackson and others on this score is that secured creditors would be mostly indifferent to a collectivizing *ex ante* agreement, provided they were assured that such an agreement would not impair their state law (Article 9) rights. *See* Jackson, *supra* note 6, at 869-70; Note, *Good Faith Inquiries Under The Bankruptcy Code*, *supra* note 11. This is a far cry from an gain" for the weal of the common pool.[106] For the Collectivists, bankruptcy law forces an alignment of circumstances that insists upon a bargain in effect, if not in reality. Bankruptcy imposes a kind of enforced Eden in which grab-bag incentives are discarded, and a debtor's assets are deployed to produce the greatest benefit to the greatest number—a notion with considerable appeal on democratic grounds, if nothing else.

The Collectivists' vision of a forced bargain is, of course, an artifice. But if bankruptcy is to yield what Collectivism regards as an efficient result, it must lead to the same deployment of the debtor's assets as would have followed from a voluntary *ex ante* bargain among creditors. In other words, apart from artificially imposing the advent of the "bargain," the bankruptcy proceeding should in all other respects emulate the particulars hypothesized for a voluntary collectivizing bargain among creditors. For the most part, this means bankruptcy must leave undisturbed the relative entitlements of all creditors under state law.[107] A re-

---

inducement to secured creditors to bargain. Accordingly, "a collective regime such as bankruptcy is necessary as a device to induce cooperative behavior." Jackson & Scott, *supra* note 6, at 137 n.2.

At the same time, the bargain is, after all, hypothetical and no more than a metaphor, *but see infra* note 148, and it would seem that so long as our purpose is to develop the dynamics of the bargain model, indifference on the part of a secured creditor will serve just as well as active interest. But once the bargain model is loosed from its hypothetical moorings, it becomes apparent that even the assumption of secured creditor indifference is no longer safe, and the model founders on the positive law in a way which severely limits its *explanatory* power. *See infra* note 117 (discussing United States Savs. Ass'n of Tex. v. Timbers of Inwood Forest Assocs., 484 U.S. 365 (1988)).

This is hardly surprising. As Professor Eisenberg has observed, "[s]tripped of real-world characteristics, hypothetical bargains struck by hypothetical actors cannot hope to capture the full range of human interaction." Eisenberg, *Commentary on "On the Nature of Bankruptcy": Bankruptcy and Bargaining*, 75 VA. L. REV. 205 (1989). Eisenberg does, however, acknowledge the important contribution of the bargain model, the discussion of which he finds "valuable because it provides a fresh outlook on difficult questions of bankruptcy theory." *Id.* In addition to critiquing the improved bargain model proposed by Jackson and Scott, *see infra* note 124, Eisenberg introduces to bargain-based theory of bankruptcy his insights on the role of *actual* bargains struck informally outside of (albeit in the "shadow of") both bankruptcy and state law formal dispute mechanisms, Eisenberg, *supra*, at 206-08. This is a contribution to the bargain theory discourse well worth study.

106 For Jackson this is again analogous to the handling of the common pool problem among competing mineral interest owners. *See supra* note 91. In that context, the common pool problem is resolved through forced (statutory) unitization.

107 It would be nonsense to suppose a creditor, secured or otherwise, would enter voluntarily into a collectivizing agreement that redistributed the debtor's assets to that creditor's disadvantage in comparison with its state law entitlements. Thus, central to Collectivism is the proposition that non-bankruptcy (state law) entitlements must be preserved in bankruptcy. *See, e.g.*, T. JACKSON, *supra* note 81, at 20-24; Jackson, *supra* note 6, at 871 (a secured creditor's state law entitlements should be preserved in bankruptcy); Eisenberg, *supra* note 86, at 953-59. In short, "[T]he cornerstone of the creditors' bargain is the normative claim that prebankruptcy entitlements should be impaired in bankruptcy *only when necessary to maximize net asset distributions to the creditors as a group* and never to accomplish purely distributional goals." Jackson & Scott, *supra* note 6, at 155-56 (emphasis added). Thus, "[c]hanges in substantive rules *unrelated to preserving assets for the collective good of the investor group* [pool of interested claimants] . . . run counter to the goals of bankruptcy." Baird & Jackson, *supra* note 6, at 101 (emphasis added).

The emphasized language in each of the above quotations indicates the Collectivists' recognition ordering of patterns of priority and distribution would likely realign creditor incentives in a manner that would induce behavior antithetical to the interest of the common pool.[108] Thus, in the terms of the bargain metaphor, bankruptcy should preserve the bargainers' pre-bankruptcy negotiating positions.

The view that maximization of asset values delimits the scope of bankruptcy policy leads to the Collectivist proposition that bankruptcy law must be confined to the realm of procedure.[109] Were bankruptcy law to become a set of substantive rules reordering creditor entitlements created under state law collection schemes, the bankruptcy process would become the target of forum shopping and the object of strategic behavior.[110] That is, a bankruptcy law with substantive policies of its own would encourage filings aimed at capitalizing on redistributive advantages.[111] Should bankruptcy law fail to replicate the milieu of the hypothetical bargain by preserving state law entitlements and priorities, creditors would have no incentive to act according to a program of concerted effort, and inefficient asset deployment would follow. An ancillary value of the creditors' bargain model, then, is its usefulness as a paradig-

---

that "[a] successful transition from the nonbankruptcy to the bankruptcy forum does not require the preservation of each detail of any given nonbankruptcy right." T. JACKSON, *supra* note 81, at 28. Given the single purpose Collectivism attributes to bankruptcy, it is sensible to preserve state law entitlements only insofar as they advance that purpose. When matters are so ordered that recognizing a state law collection right would prove antithetical to the maximum deployment of the debtor's assets, the state law entitlement must yield. Thus, it becomes "necessary to weigh the damage that recognizing a particular nonbankruptcy right would cause to collective action against the cost of any incentives that would be potentially created by upsetting that right." *Id.* (On the matter of "the costs of any incentives that would be . . . created," see *infra* note 108).

It is not possible literally to preserve state law entitlements in bankruptcy (*e.g.*, a secured creditor cannot in bankruptcy foreclose on the collateral in the teeth of § 362(a) of the Bankruptcy Code). What matters is preserving the "relative value" of the state law entitlement, T. JACKSON, *supra* note 81, at 29, although even the relative value of the right might be sacrificed on the altar of maximum deployment, *id.* at n.15.

108 Given a fixed pool of assets and a fixed number of claimants among whom those assets are to be distributed, a change in distribution schemes necessarily entails a transfer of wealth from some claimants under the old scheme to other claimants under the new. It is self-obvious that claimants would elect the scheme of distribution under which they were the beneficiaries of that transfer and eschew that under which they were benefactors. Where state law and bankruptcy law offer not just alternate collection schemes but alternate patterns of distribution as well, the decision to enlist one regime or the other will be made strategically without appreciation for the maximum deployment goal. *See* Jackson & Scott, *supra* note 6, at 156 n.2; Baird & Jackson, *supra* note 6, at 101. The result, simply put, is forum shopping. *See* Baird, *supra* note 81, at 824.

On the matter of a secured creditor's state law entitlements in bankruptcy, see *infra* note 117 and accompanying text.

109 *See, e.g.*, T. JACKSON, *supra* note 81, at 5: "[T]he remaining principal role of bankruptcy law has been and should be more procedural than substantive." *But see* Warner, *supra* note 105, at 491 ("The most striking feature of Jackson's view is that it leaves the mere husk of bankruptcy law intact. Devoid of any substantive content, bankruptcy becomes nothing more than a procedural device to bring creditors together and force them to do what is in their [collective] best interest.").

110 *See supra* note 108.

111 *Id.*

matic ideal against which to measure the set of rules presently controlling the bankruptcy process to determine the extent to which they emulate the bargain, and thereby advance Jackson's first principle of bankruptcy.[112]

If we are willing to embrace Collectivism, we have, at least, the first clear beginning point for analysis of the good faith cases.[113] From the perspective of a single, debt collectivizing principle, it follows that cases not presenting a common pool problem have no business in bankruptcy. Insofar as they are filed with ends in mind other than the resolution of a common pool problem, petitions for bankruptcy relief should be dismissed as attempted misuses of the process.[114] Indeed, Jackson seems to regard the frequency with which courts have used the good faith doctrine to deny access to bankruptcy as evidence that those courts are of one mind with him in supposing the sole concern of bankruptcy to be debt collectivizing.[115]

If the courts agree that the sole concern of bankruptcy is as Jackson describes it, however, it seems ironic that they also have been charged with creating the very conditions thought by the Collectivists to provoke secured creditors to make good faith challenges. Were secured creditors awarded lost opportunity costs in the course of a reorganization, their relative entitlements would be unaffected by the proceeding. Preservation of secured creditors' rights, in turn, would eliminate the prospect of redistribution at their expense.[116] Thus, if secured creditors received lost opportunity costs in the course of reorganization, no strategic advantage would be had of them in bankruptcy. If the strategic advantage to be gained at the expense of secured creditors were extinguished, petitions filed to secure that advantage would disappear, along with, ipso facto, the need to determine whether or not those petitions were filed in good faith.[117] The numerous good faith challenges made by secured creditors thus serve as striking illustrations of the Collectivist notion that an opportunity for redistributive advantage is never lost on the relentless redis-

---

112 Whether the creditors' bargain model is an attempt to describe positive bankruptcy law in the abstract or an elaborate heuristic to develop normative principles is a question addressed *infra* at note 148.

113 *See supra* note 82 and accompanying text (commenting that the literature on bankruptcy policy has been, until recently, exiguous).

114 *See* T. JACKSON, *supra* note 81, at 199. *See also id.* at 193-94 (discussing *In re* Tinti Constr. Co., 29 Bankr. 971 (Bankr. E.D. Wis. 1983)). *Cf.* Note, *Good Faith Inquiries Under the Bankruptcy Code*, *supra* note 11, at 813-16 (arguing that good faith challenges to petitions could frequently be avoided if secured creditors' state law rights were preserved and strategic advantages to other claimants thereby eliminated). *See generally infra* note 117.

115 *See* T. JACKSON, *supra* note 81, at 195.

116 *See supra* note 108.

117 But for the automatic stay, a secured creditor could foreclose its security interest, sell the collateral, and reinvest the proceeds at a profit determined by investment conditions at the time. To preserve the relative value of the secured creditor's claim in bankruptcy, according to the Collectivists, secured creditors should receive lost opportunity costs occasioned by the stay. Otherwise, the

tributive impulses of creditors in general. Yet, these challenges hardly stand as overwhelming testimony to widespread concurrence by bankruptcy judges with the entirety of Collectivist theory.

In any event, from our brief excursus into Collectivism, we can identify two conclusions that are relevant to any inquiry into the good faith filing requirement. First, to say that a case was filed in bad faith is to say that the petition proposes a misuse of the bankruptcy laws.[118] Second, a case filed where there is no common pool problem to contend with is a fortiori such a case.[119]

There is much of value in the work of the Collectivists. It reminds us, for instance, that an original purpose of the bankruptcy process is efficient debt collection in multi-default cases where there simply are not enough fish and loaves to go around. In an era of mega-reorganizations motivated by a staggering array of novel impulses,[120] it is worthwhile periodically to revisit that touchstone.[121] The Collectivists revive our awareness of the importance of an original historic function of bank-

---

opportunity is forfeit and is used, in effect, to underwrite the debtor's reorganization for the benefit of unsecured creditors who are functionally the new owners of the business.

On these grounds, the Collectivists insist that a secured creditor's interest is adequately protected in bankruptcy pursuant to § 362(d) only if the creditor receives lost opportunity costs from the estate to reflect what the secured creditor would have realized on reinvesting the proceeds from the sale of the collateral in some new opportunity. Anything less and the secured creditor is entitled to relief from the stay. *See generally* T. JACKSON, *supra* note 81, at 183-90. For a time, it seemed the Collectivist view on lost opportunity costs was gaining ground. *See, e.g.*, Crocker Nat'l Bank v. American Mariner Indus. (*In re* American Mariner Indus.), 734 F.2d 426 (9th Cir. 1984) (adequate protection requires that an undersecured creditor is entitled to lost opportunity costs). However, the advance in that direction was halted by the Supreme Court. *See* United States Savs. Ass'n of Tex. v. Timbers of Inwood Forest Assocs., 484 U.S. 365 (1988) (undersecured creditors are not entitled to lost opportunity costs arising from the delay in payment occasioned by bankruptcy). For a discussion of *Timbers* and Norwest Bank Worthington v. Ahlers, 485 U.S. 197 (1988), suggesting that these two recent decisions, although having confounded and confused the law of bankruptcy, still may be reconciled with core bankruptcy policy, see Scott, *supra* note 84; *see also supra* note 35 regarding the treatment of secured claims in bankruptcy.

One commentator has urged that if secured creditors received lost opportunity costs, thereby preserving the relative value of their state law entitlements, *see generally supra* notes 107 & 108, good faith filing challenges raised by secured creditors would be avoided altogether. Without a redistribution of the lost opportunity value, secured creditors would be indifferent to the collective proceeding imposed by bankruptcy. *See* Note, *Good Faith Inquiries Under the Bankruptcy Code*, *supra* note 11, at 801. Jackson is of the same mind. *See* T. JACKSON, *supra* note 81, at 195; *see also* Jackson's approving citation to the above-mentioned Note, *id.* at n.8.

For a thorough, well-considered treatment of post-petition interest for undersecured and oversecured creditors, see Carlson, *Postpetition Interest Under the Bankruptcy Code*, 43 MIAMI L. REV. 577 (1989).

118 *Id.* at 196 ("Good faith is simply a label for those cases in which a bankruptcy proceeding is appropriate.").

119 *See supra* note 84 and accompanying text; *see also supra* notes 89 & 90.

120 *See generally* Kennedy, *supra* note 8. *See also infra* note 188 and accompanying text discussing the place of multifarious filing motives in the good faith analysis of petitions.

121 Warner, who has criticized Jackson for failing "to prove his main point," Warner, *supra* note 105, at 489, nevertheless finds Jackson's "reminder" to be helpful, *id.* at 492.

ruptcy[122] and, in the rejuvenating light of fresh analysis, transform it from a rarely consulted premise to a vital consideration that figures actively in current issues of pressing importance. In short, the Collectivists offer both a fresh perspective on the role of the debt collectivizing purpose of bankruptcy and a coherent, vigorous methodology for assessing the extent to which bankruptcy law advances or fails that purpose. Even commentary otherwise critical of Collectivism routinely acknowledges this contribution.[123]

Notwithstanding its positive aspects, Collectivism has been sharply criticized of late on different fronts. Some attacks are mounted in the argot of Collectivism itself, consisting of charges of internal inconsistencies in the system.[124] These need not detain us. We are concerned here with challenges to Collectivism on an ideological level—challenges to ba-

---

122 Not every commentator agrees with Jackson that debt collectivizing was the single historic function of bankruptcy. *See id.* at 491 n.4.

123 *See, e.g.*, Warren, *supra* note 82, at 813.

124 *See, e.g.*, Warner, *supra* note 105, at 493 (criticizing Jackson's theoretical postulates and conclusions partly on grounds of internal inconsistencies: "Whenever his common pool theory threatens a [bankruptcy] rule he agrees with, he pulls from his hat some other justification for the threatened rule."). The most complete discussion of Jackson's LOGIC AND LIMITS to date is found in Carlson, *Philosophy in Bankruptcy*, *supra* note 103. The reviewer unremittingly and, we would add, skillfully challenges ideological and methodological principles that are the plinth of the Bargain Model.

In their joint work, *On the Nature of Bankruptcy: An Essay on Bankruptcy Sharing and the Creditors' Bargain*, *supra* note 6, Scott and Jackson have sought to enrich the bargain model. Basically, the creditors' bargain model is repostulated in an "expanded framework" to explain away the apparent contradiction of the central premise of the bargain model with what amounts to redistributional rules and impulses at work in the bankruptcy law. *Id.* at 157. Under the regime of the new and improved creditors' bargain model, "all participants share . . . the risks of business failure attributable to certain 'common disasters' . . . . [D]istributional effects premised on the anticipation of these common disasters would be explicitly included in an ex ante bargain . . . ." *Id.* (footnote omitted).

On the Nature of Bankruptcy seems mainly to adopt a perspective from which to survey the bankruptcy process at a point further removed from that adopted by Jackson in his earlier work. The insistence on one goal for bankruptcy is no less single-minded, but it seems that Scott and Jackson have undertaken to view the bankruptcy process in the round, so to speak, to dispel inconsistencies between theory and practice as merely the product of an earlier narrower vision of the legal landscape. *But see* Eisenberg, *supra* note 105, at 212:

> [T]heir discussion provides some support for the modified creditor's bargain. The kind of ringing, conclusive support one might hope for is, however, lacking. And little of the support that is marshalled suggests that the modified creditor's bargain is superior to the simpler theories that might underlie much of bankruptcy law.

To be sure, a broader view of the legal landscape reveals new insights and suggests relationships theretofore unrecognized or only dimly perceived. Yet, it may be that expansion of the bargain model dilutes the theoretical prowess of the model in making it appear equivocal or uncertain. *Cf.* Warner, *supra* note 105, at 493 ("It is impossible for the reader to guess in advance which rules . . . [Jackson] will keep and which he will discard. Perhaps, Jackson's perfect bankruptcy law actually incorporates more than one policy.").

Warren similarly has accused Baird of inconsistency in his theoretical position. *See* Warren, *supra* note 82, at 803 ("As Baird has used it . . ., collectivism is nothing but a veil to conceal his relentless push for single-value economic rationality, an excuse to impose a distributional scheme without justifying it.").

sic assumptions and conclusions and to the impact of its methodology. Collectivism's chief ideological rival consists of several assumptions that together comprise what earlier was referred to as the Traditional view,[125] a term we use in an effort to group those assumptions under a single, wieldy heading.

As we see it, the principal point of contention between the Traditional and the Collectivist views is whether the sole purpose of the bankruptcy process has been and is debt collectivizing. The proponents of the Traditional view do not claim that debt collectivizing is not important;[126] but they deny that it is the only purpose or, for that matter, that it is always the most important or worthy.[127] Rather, it is proposed that while debt collectivizing is always relevant in bankruptcy, it can be sacrificed when necessary to achieve other goals and purposes of the bankruptcy process. This follows from the idea that the bankruptcy milieu requires careful attention to a host of interests and concerns largely unaffected in the state law debt collection milieu.[128] Outside of bankruptcy, the impact of the state law collection systems is measurable by reference to a closed and readily identifiable community of creditors;[129] it is an arena peopled only by individual creditors seeking the enforcement of rights arising from voluntary exchange transactions during the lifetime of the debtor enterprise.[130] A debtor may have several creditors, each seeking to satisfy a claim; but so long as their actions against the debtor do not engender a collapse of the firm, these are essentially individual dramas in which are sorted out the rights of creditor versus debtor.[131]

---

125 *See supra* note 85.

126 *See, e.g.*, Warren, *supra* note 82, at 800 ("Collectivism provides a useful way to examine *some* bankruptcy problems. Baird shows how the need for collectivism can explain why the bankruptcy system substitutes a single, lower-cost action for expensive, multiple individual actions.") (emphasis added) (footnote omitted).

127 *See id.* at 78 (discussing the role of bankruptcy in an "integrated system"). Warren observes:

> Professor Baird and I hold very different views of the purpose bankruptcy law serves. I see bankruptcy as an attempt to reckon with a debtor's multiple defaults and to distribute the consequences among a number of different actors. Bankruptcy encompasses a number of competing—and sometimes conflicting—values in this distribution. As I see it, no one value dominates . . . .

Id. at 777 (footnotes omitted).

128 Professor Warren states that:

> [a] central purpose of state debt collection law is to provide a means for collection of a single unpaid debt. State collection law swings into action on the complaint of a single creditor, and it provides that creditor an avenue to pursue payment of the obligation owed to it. In enforcing the rights of one creditor, state collection law does not address the possible consequence that the collection will render the debtor unable to pay its remaining creditors.

Id. at 782.

129 "A complex factual inquiry into the consequences for others of the collection of the single debt need not be a part of every collection lawsuit." *Id.*

130 Warren sees debt collection systems, whether established by bankruptcy law or state law, as best discussed in the context of contract, "the prototype for most debtor-creditor relations." *Id.* at 778 n.7.

131 *See id.* at 782-85. We might say that state collection law is principally a matter of creditor

In sharp contrast to the individual squabbles between debtors and creditors which are adequately addressed by state law is the case of complete firm failure. This scenario has been more graphically described as a common disaster[132] in which a broad range of interests are implicated, only some of which are claims of creditors having distributive rights and remedies under state law.[133] State law collection systems lack the sophistication to accommodate and effectively sort out interests other than those of conventional creditors created under the state law system itself.[134] If bankruptcy is nothing more than a federal debt collection system—that is, if it is simply an alternative to state debt collection as the Collectivists would have us believe[135]—then bankruptcy will prove no more adroit, or for that matter interested, than state law in responding to non-creditor and multi-creditor interests implicated in firm failure. The Traditional view envisions a greater role for the bankruptcy process. It avoids relegating the bankruptcy process to the status of a mere alternate debt collection device by seeking to protect the interests of non-creditors (in the usual sense), victims of firm failure who would otherwise lack a champion.[136]

By providing for the interests of non-creditors, the Traditional view recognizes that the financial collapse of a firm presents questions of loss allocation and community interest simply not implicated in individual

versus debtor, although state law collection rules certainly bear on the collection rights of creditors of the same debtor *inter se* (*e.g.*, Article 9 secured creditors have priority over unsecured creditors).

132 This useful metaphor was first suggested by Scott in *A Relational Theory of Secured Financing*, 86 COLUM. L. REV. 901, 967-68 (1986). The concept is requisitioned as part of the effort to enrich the bargain model in Jackson & Scott, *supra* note 6, at 157 & n.4.

133 *See* Warren, *supra* note 82, at 788 (discussing congressional comments on the Bankruptcy Code). *See generally infra* note 138. The parties affected by a bankruptcy filing may be strikingly dissimilar in several ways. Some are not creditors at all, but nevertheless feel the impact of a filing. For example, the participants in a local economy in which an important debtor enterprise has operated are undeniably affected by the failure of that debtor. Other affected parties may be creditors with claims against the debtor cognizable in bankruptcy, but who did not choose to deal with the debtor in the first place. Tort claimants are illustrative of this group. Neither affected parties without claims, nor parties with claims who never voluntarily chose to deal with the debtor enterprise, seem to fit into the regime of the hypothetical creditors' bargain model.

For a discussion of the varying consequences of the distribution of a debtor's wealth on different sorts of creditors under recently enacted judgment lien statutes, see Woodward, *New Judgment Liens on Personal Property: Does "Efficient" Mean "Better?"*, 27 HARV. J. ON LEGIS. 1, 31-33 (1990).

134 Warren describes this inadequacy in the following terms: "the state law system is *not* well-suited to . . . [the] circumstances [of a debtor's collapse] . . . because it necessarily must consider too broad a range of possible debtor-creditor relationships and follow collection principles inconsistent with those raised in the circumstances of complete collapse." Warren, *supra* note 82, at 783 (emphasis in original).

In contrast to state law on this score, consider that bankruptcy law recognizes the rights of those with future tort claims not cognizable under state law collection systems. *See id.* at 756.

135 *See supra* note 84 and accompanying text.

136 "Congress . . . accepted the idea that bankruptcy serves to protect interests that have no other protection." Warren, *supra* note 82, at 788.

debtor-creditor disputes.[137] For this reason, the Traditionalist believes that the bankruptcy system is and should be designed to address a broad range of interests affected by the collapse of a debtor enterprise. This broad range should include, but not consist exclusively of, the interests of creditors with unpaid state law claims.[138] Brought within the bankruptcy process, diverse interests can be taken into account and, perhaps, protected and accommodated collectively under the auspice of the proceeding itself.[139]

For present purposes, it is important to keep in mind mainly that the Traditional view regards bankruptcy as responsive to the needs of a great variety of sometimes unrelated, and not infrequently antithetical, interests.[140] In any given case, it may be that all these interests have no more in common than vulnerability to the collapse of the debtor enterprise. Thus, it is hardly remarkable that the underlying purposes and ends of the bankruptcy process are, according to the Traditional view, correspondingly various and cannot be presumed to bear a rational relation to one another.[141] To couch these postulates in terms nearer to those we develop in this Article, we would say that the parameters of bankruptcy policy are established by courts according to the purposes that the bankruptcy process must answer in a given case. While these purposes may be loosely organized under the heading of bankruptcy policy, this in itself does not indicate the presence of a formally elegant, unified system.[142] According to the Traditional view, the only "system"

---

[137] *See id.* at 781, 783-84.

[138] Employees, trade creditors, and a variety of other constituencies are often affected by firm collapse. *See generally*, Warren, *supra* note 82, at 787-88. The Collectivists by no means deny that the failure of an enterprise may have deeply felt and far reaching impact. *See, e.g.*, Baird & Jackson, *supra* note 6, at 101-02.

[139] At least one other commentator seems to agree that the orderly procedural regime of bankruptcy may be well-suited to solve a variety of institutional problems. *See* Warner, *supra* note 105, at 496. For that matter, bankruptcy may, from time to time, offer the only forum to deal with institutional problems. *See infra* notes 144-46 and accompanying text.

[140] According to Warren, bankruptcy distributes the cost of enterprise failure among interested parties according to priorities based upon a number of key factors, including: (1) Relative ability to bear the cost of default; (2) Incentive effects on pre-bankruptcy transactions, (*i.e.*, exceptions to the preference rule of § 547(b) for transactions immediately preceding bankruptcy that might keep the debtor firm alive); (3) Similarities among creditors; (4) Equity owners bear the loss of business failure; (5) Benefit to the bankruptcy estate of reordering or impairing a non-bankruptcy entitlement to enable the survival of the debtor's business (*e.g.*, executory leases may be assumed or rejected according to the best interest of the debtor's business notwithstanding the lessor's rights in the lease that would otherwise be enforced under state law). *See* Warren, *supra* note 82, at 790-93.

[141] *See id.* at 795-97.

[142] "My approach does not assume that current bankruptcy policy is unfailingly rational, either normatively or empirically." *Id.* at 797.

In discussing Norwest Bank Worthington v. Ahlers, 485 U.S. 197 (1988), Professor Ayer opined:

> I have suggested a lack of controlling "theory" in this realm. On the other hand, I have not tried to supply any such theory, nor do I lament the possible absence of one. The effort to articulate "theory" for bankruptcy . . . is certainly alive and well, but theorizing requires theo-

at work in the law of bankruptcy is one that provides for the case-by-case adjustment, realignment, and reformulation of bankruptcy purposes along functional lines. It seems fair to state, then, that the Traditional view regards the central purpose of bankruptcy, if it can be called that, as the apportionment of losses occasioned by firm collapse according to a set of principles, none of which is pre-eminent by definition.

B. A Diverging Analysis of the Scope of Bankruptcy Policy

Having outlined briefly the Collectivist and Traditional views, we turn to our perspective on the question of underlying purpose in bankruptcy. That perspective is born of a jurisprudential turn of mind that may be expressed in a few basic notions that guide our analysis. First, we assume that no fixed purpose or even set of purposes is discoverable or, for that matter, immanent in the law of bankruptcy. To state the matter more robustly, we deny the permanent hegemony of an original first principle and, concomitantly, of a systematically knowable, ideal bankruptcy policy at work that is merely imperfectly expressed in bankruptcy law. The search for an immutable, ideal purpose or set of purposes is, therefore, necessarily an exercise in normative advocacy, not discovery.

In stating this proposition, we do not mean to imply either that the construction of normative principles of bankruptcy is irrelevant or that engaging in purely abstract theoretical analysis is a fruitless exercise. To the contrary, we believe that normative postulates have their place and that it is a healthy and valuable exercise to test the provisions of the current law for consistency with those postulates once they have been identified and articulated. Collectivism, for instance, has provided us with a useful way of thinking and talking about the efficacy of particular bankruptcy rules which sharpens the focus and adds critical insight to the process of considering proposals for positive law reform. We simply wish to be understood as suggesting the inherent limitations of any closed-end theory or understanding of the law. The reality of a legal process, particularly one as complex as bankruptcy, is simply that it is not susceptible of reduction, except in theory, to a single ideal or objective, no matter how ideologically well grounded or logically compelling that ideal or objective might be.[143]

> retical justification. And at least in this realm [*i.e.*, the issues in *Ahlers*], Congress and the courts have proven uniquely resistant to pressures to organize their work under any grand design.
>
> . . . [T]he work product of both the courts and Congress may bespeak a conviction that bankruptcy law is too complex for facile categorization.

Ayer, *Rethinking Absolute Priority after Ahlers*, 87 MICH. L. REV. 963, 1025 (1989) (footnotes omitted).

143 *Cf.* Gilmore, *Product Liability: A Commentary*, 38 U. CHI. L. REV. 103, 116 (1970) (suggesting a similar view about the utility of legal theory and its relationship with actual events). As to whether Collectivism proposes a set of normative principles and critique of positive bankruptcy law, or whether it proposes a descriptive paradigm, see *infra* note 148.

The absence of an ideal or otherwise ordained purpose, therefore, advises caution in valuing the historically original purpose of bankruptcy. If there is no "right answer" to be had, then it is no sooner to be had in the remote past than in the present. Again, this is not to suggest that study of original or early purposes of bankruptcy is not worthwhile. It simply means that tracing bankruptcy policy to its origins is the beginning, not the end, of the inquiry, and those original purposes are to be valued primarily for the light they cast on the shadowy question: What have the purposes of bankruptcy become?

That question, of course, anticipates a second basic idea at the bottom of our analysis. We believe bankruptcy to be a problem-solving institution,[144] the purposes of which are in a constant state of flux under the watchful eye of the judiciary.[145] The set of purposes is never closed either as to number or kind, but constantly evolves in measured response to similarly emerging eventualities of commercial endeavor.[146]

An important corollary to the notion of an evolving set of purposes is the singular role of the courts in the process. It is the judiciary, far more than Congress, which controls the evolution of bankruptcy policy. That the courts must both administer and declare the purposes of bankruptcy leads to our third fundamental assumption: there is no such thing as a bankruptcy purpose with an existence independent of the judicial process in the form of bankruptcy proceedings. Bankruptcy purposes are considered and reconsidered, formulated and reformulated, from one proceeding to the next.[147]

This leads to our final basic assumption, namely, that the evolution of purpose is describable. Of course, this is the singular advantage of disabusing ourselves of the idea that bankruptcy purposes exist other than as they are announced in cases. It is a function of the freedom gained in breaking off the search for an ideal purpose or set of purposes. We are free to sample the system at any given point to enlighten ourselves as to the then-current state of the evolutionary process.

With these four basic assumptions in mind, it is worth returning briefly to consideration of the Collectivist and Traditional views. As to Collectivism, our basic assumptions earlier drove us to reject the pros-

---

144 *See generally infra* text accompanying notes 157-58.

145 On the role of the judiciary, see *infra* notes 147 & 164 and accompanying text.

146 We are acutely aware, of course, that we do not state a new philosophical position here. Certainly, we share a great deal with the Realists, most notably Karl Llewellyn. For an intriguing discussion of, among other things, the Realist movement, see G. GILMORE, THE AGES OF AMERICAN LAW 81-86 (1977). For a fascinating discussion of Llewellyn, his philosophy of law, and principle works, see W. TWINING, KARL LLEWELLYN AND THE REALIST MOVEMENT (1973).

147 We do not wish our emphasis on the role of the courts to be mistaken for the suggestion that everything important in the bankruptcy process can be learned from cases. To the contrary, we believe the forces shaping and reshaping bankruptcy policy are exogenous, arising from, for example, market institutions. Our position is that courts are often the focal point where those forces converge to exert continuous pressure for change.

pect of a single purposive object of bankruptcy. If debt collectivizing was the original, historical purpose, it is none the worthier for it. Whether it *should* be the sole purpose we do not debate here, but that it *is not* we believe to be beyond argument. This does not entail the rejection of the body of the work of the Collectivists. Far from it. While we decline to discuss in detail points of compatibility and points of departure,[148] it is enough to say that if not the sole function of bankruptcy, debt collection

[148] While we have said we do not wish to debate the operational details of Collectivism, we do believe it important to call attention to an aspect of the Collectivist endeavor that we find bothersome. The fact is, we are unable to decide with any certainty whether Collectivism is a blueprint for the law of bankruptcy or an attempt to allegorize the positive law to facilitate the systematic understanding of it. If it is the former, there must be some justification for the normative central premise—why should debt collectivizing to maximize efficient asset deployment be the sole function of bankruptcy to the exclusion of other worthy purposes we might imagine? *Cf.* Warren, *supra* note 82, at 803, 808, 812-13.

If, on the other hand, Collectivism is an attempt at systematic description to bring order to the positive law through heuristic conceptual models, what are the Collectivists describing? As a descriptive model, Collectivism does not provide a particularly able explanation of the case law. For instance, its descriptive powers wither before United Savings Association of Texas v. Timbers of Inwood Forest Associates, 484 U.S. 365 (1988), which starkly denies the central idea of Collectivist thought: that secured creditors should receive lost opportunity costs in bankruptcy. *See supra* note 117 and accompanying text; *cf.* Scott, *supra* note 84 (addressing *Timbers*'s impact on and relationship to bankruptcy policy). We know from Jackson only that debt collectivizing for maximum asset deployment is the "historic function" of bankruptcy, a notion he seems to have gleaned from early case law. *But see* Warner, *supra* note 105, at 491 n.4. If so, then Collectivism describes what may have been the sole function of bankruptcy, but the decision to limit the purpose of bankruptcy according to that early statement is no less in need of justification on policy grounds than if the sole function is stated as an original normative proposition. Early case law has nothing particularly to recommend it over later case law for being early. For an alternative view concerning the determination of bankruptcy purposes, see *infra* notes 156-64 and accompanying text.

Finally, there is little in the scholarly literature of Collectivism from which to formulate a confident statement of the broad object of Collectivist inquiry. Jackson and Scott once indicated that the work of the former, embodied in T. JACKSON, *supra* note 81, had sought "to develop a conceptual model with a clear normative perspective" against which "to consider whether the bankruptcy process either reflects or deviates from the stated norm." Jackson & Scott, *supra* note 6, at 158 n.5. In their joint effort to "provide a richer normative theory" than that offered by Jackson's work, on the other hand, Jackson and Scott thought that object could best be accomplished "by enhancing the explanatory power of the original model" through "a positive analysis of the bankruptcy process." *Id.*

How it is that the normative worth of the bargain model is accentuated by enhancing its explanatory power we are not equipped to say. As to Jackson and Scott, they only remark cryptically that "the distinction between those two approaches is not as clear as their several adherents would assert," and that "[t]his should not surprise anyone who subscribes to the view that persistent social institutions rest on purposive foundations." *Id.* We find it interesting that one of those "several adherents" seems to include a fellow Collectivist. *See* Baird, *supra* note 81, at 817 ("Warren seems to derive what bankruptcy law ought to be from what it is, but one cannot derive the normative from the positive.").

Scott, in *Sharing the Risks of Bankruptcy:* Timbers, Ahlers, *and Beyond*, *supra* note 84, at 185-86 n.7, addresses the "nature and function of legal theory" in general terms, stating, "[t]he question for any theory is not whether the particular stories or abstractions approximate reality . . . . Rather, the question is whether the theory tells us something about the reality that is useful to know." We certainly do not disagree with Scott on this point, but we find it offers little by way of a definitive is always an important one. To this we would add that Collectivism, through its methodology and insightful heuristic, offers the most penetrating analysis in the literature of questions relating to the advancement of a "first principle of bankruptcy." Thus, we view the work of the Collectivists as the most important treatment of one, and perhaps even the most basic, of bankruptcy's purposes. However, the question Collectivism cannot by definition answer through its methodology is, what *are* the purposes of bankruptcy?

The Traditional view, it will be recalled, rejects the central premise of Collectivism on the grounds that bankruptcy necessarily serves an eclectic, loosely related set of purposes in accordance with the variety of interests implicated in firm or enterprise failure.[149] Of course, in simply urging that many purposes rather than one purpose are served in bankruptcy, the Traditional view does not propose a teleology or theory of bankruptcy policy, but neither does it purport to do so.[150] The Traditional view, to the extent it has been recently developed in the literature at all, was developed only in the course of rejecting the unified system of the Collectivists.[151] In so doing, its spokesperson[152] openly denied the

statement of the mission of Collectivism beyond that Collectivist inquiry is a useful aid to understanding some theory about one purpose of bankruptcy law.

The point we wish to make in this digression is not that Collectivism is carelessly formulated, lacks depth, or is necessarily unconvincing. Rather, we simply believe it important to call attention to what appears as the absence of a clear statement of, or perhaps lack of consensus on, the mission of Collectivist inquiry.

149 *See supra* notes 127 & 128 and accompanying text.

150 "I have offered a dirty, complex, elastic, interconnected view of bankruptcy from which I can neither predict outcomes nor even necessarily fully articulate all the factors relevant to a policy decision." Warren, *supra* note 82, at 811. Warren further states, "I cannot claim that bankruptcy, at its heart, is an intellectual construct or that I can reason to a meaningful conclusion by doing nothing more than thinking hard about logical consequences derived from a handful of untested assumptions." *Id.* at 812.

151 Before proceeding to a direct challenge of Baird and Jackson's Collectivism, Warren develops her position in *Bankruptcy Policy*, *supra* note 82. Baird responds to Warren in *Loss Distribution, Forum Shopping and Bankruptcy: A Reply to Warren*, *supra* note 81. Warren's effort in *Bankruptcy Policy*, however, is much more than a reply or challenge to Collectivism. While it does not propose a unified theory to explain bankruptcy, much of that article is devoted to a fairly complete and well considered discourse on Warren's views on the basic purposes and function of bankruptcy law. This discussion is carefully developed against the background of state law default and collection. The Warren and Baird debate is well worth reading for its discussion of the different roles played by the bankruptcy collection system on the one hand, and the state law collection system on the other.

152 Again, we award this role to Warren without having consulted her, and largely because in her debate with Baird, hers is referred to as the Traditional view. *See* Baird, *supra* note 85. Whether or not Warren states the Traditional view in *Bankruptcy Policy*, *supra* note 82, or, for that matter, whether there indeed *is* an identifiable Traditional view are questions of no particular consequence. It is infinitely more important that Warren has collected together and organized a number of basic postulates for the purpose of making a self-conscious, systematic statement about bankruptcy policy that does not rest on premises of finance theory. This is not to denigrate approaches that do proceed from that basis. It is only to indicate that the additional perspective is welcome to enrich discussion and inquiry in an area that is underdeveloped.

possibility of a formal system for bankruptcy, a process she characterized as largely aimed at achieving an orderly and equitable accommodation of a host of disparate, even antithetical interests.[153]

In any event, our own conclusions drawn from the good faith cases are certainly consistent with an important precept that we attribute to the Traditional view: a nagging distrust of any all-embracing, formal model of bankruptcy law and policy.[154] This suspicion naturally attends the conviction that the purposes of bankruptcy are several and varied. These purposes form the ever-shifting basis upon which bankruptcy courts must act to sort out and order a broad spectrum of interests clamoring for protection in the bankruptcy proceeding.

As noted earlier, however, we would take the eclecticism of the Traditional view a step further by declaring that the purposes of bankruptcy are not only several and varied, but are also in a state of continuous change orchestrated by the courts.[155] A critical task for the courts in the bankruptcy process is to determine which eventualities should be attended to by bankruptcy law; that is, it is the business of the courts to decide the purposes to be served by bankruptcy when cases are challenged as inappropriate to the bankruptcy forum.[156] With that, we turn to the concrete application of these principles in the good faith cases.

III. TOWARD AN ALTERNATIVE UNDERSTANDING OF THE GOOD FAITH DOCTRINE IN BANKRUPTCY

A. *Role of Bankruptcy and the Bankruptcy Courts*

The role of bankruptcy as a forum for coordinating the collection efforts of multiple creditors can hardly be ignored. Nevertheless, however desirable (or doctrinally appealing) it might be to limit bankruptcy to a single purpose such as debt collection, the fact remains that courts have shown no inclination to reduce the number or limit the kinds of problems brought to the bankruptcy forum according to a single, agreed-upon fundamental principle. For better or worse, bankruptcy has evolved into a legal institution to which commercial concerns, both large and small, have turned to resolve basic business and economic problems that are not satisfactorily addressed elsewhere. In many instances, these problems are related only incidentally, if at all, to the problems of default and immediate financial ruin.[157] The pace and complexity of modern commercial life have created enormous pressure for a system in which a

---

153 *See supra* notes 136-38 and accompanying text.

154 *See generally* Warren, *supra* note 82, at 813 (discussing limitations of an exclusively economic analysis of bankruptcy).

155 *See supra* text accompanying notes 144-47.

156 This brings up another reason why the most fully developed formal model, even one with nearly complete explanatory power, would be of limited utility. However powerful, correct, or valid, it simply would not endure.

157 *See supra* note 59.

broad range of competing concerns and interests can be factored into specific solutions which are unattainable (or attainable only at the cost of unacceptable delay) under applicable non-bankruptcy law and procedure. This system failure may result from either the unanticipated magnitude of such problems or their currency.[158]

This is not to say that bankruptcy represents the only or the best forum for responding to these problems. As has been aptly noted, bankruptcy is not a mandatory process into which all like situations can be channeled.[159] Moreover, it is entirely possible that problems now considered appropriate for resolution in the milieu of bankruptcy ultimately may be wrested from the bankruptcy forum once the will of the body politic is clearly articulated or alternate mechanisms for resolution are forged. For example, it may well be that, as a consequence of cases like *Manville* and *A.H. Robins*, non-bankruptcy palliatives for massive tort liability claims will be forthcoming.[160] Nevertheless, to recognize that

158 Certainly Chapter 11 cases such as Manville and Robins, involving massive numbers of individual products liability claims, would be representative of instances where the sheer size and scope of the difficulties faced by a company rendered the traditional mechanisms for resolving such problems unresponsive to the needs of both the company and the claimants as a group. *See* Roe, *Bankruptcy and Mass Tort*, 84 COLUM. L. REV. 846 (1984) (pointing out that the existing tort system cannot adequately address the questions raised by massive enterprise liability for dangerous products); Bulow, Jackson & Mnookin, *Winners and Losers in the Manville Bankruptcy*, Wall St. J., Nov. 4, 1982, at 30, col. 3 (pointing out that the Manville filing would assure that future victims would not be left remedyless because prior claimants had exhausted the company's resources). In contrast, filings by companies like Eastern Airlines and Public Service Co. of New Hampshire illustrate cases brought about largely by unsettled financial and related complications resulting from questions of public policy and public interest: in these instances, respectively, airline deregulation and nuclear energy regulation. *See* Cuevas, *supra* note 82, at 315.

159 Professor Baird emphasizes this point in defense of his and Jackson's position that distributions should be made in accordance with a single set of rules. Baird, *supra* note 81, at 817-19.

160 Several proposals have been advanced for a legislative solution to the problem of processing the claims, and compensating the victims, of asbestos exposure and other mass torts. *See, e.g.*, Barth, *A Proposal for Dealing with the Compensation of Occupational Diseases*, 13 J. LEGAL STUD., 569, 576-77 (1984) (proposing extension of the principles underlying existing workers' compensation statutes to establish a no-fault insurance scheme); Note, *Mass Tort Claims*, *supra* note 54, at 1344-52 (advancing taxpayer-funded and insurance-funded plans as a more appropriate solution than bankruptcy reorganization to the problem of overwhelming tort liability); Comment, *Liability Insurance for Insidious Disease: Who Picks Up the Tab?*, 48 FORDHAM L. REV. 657 (1980); *see also* Kennedy, *supra* note 8, at 209 (noting Congress's reluctance to acknowledge any responsibility in the area or otherwise fashion any positive law solution); Roe, *supra* note 158, at 917-20 (proposing amendment of the Code to permit early initiation of a bankruptcy reorganization by companies faced with large numbers of existing and future tort claims); Wellington, *Asbestos: The Private Management of a Public Problem*, 33 CLEV. ST. L. REV. 375, 385-90 (1984) (discussing the efforts undertaken shortly after the Manville filing by asbestos producers, large insurance companies, and prominent plaintiffs' asbestos personal injury lawyers to create a private administrative agency to promote the fair settlement and efficient handling of asbestos-related claims). In his essay, Professor Wellington stressed the practical and economic inadequacy of the civil litigation process to deal effectively with the fallout resulting from the studies discovering the link between respiratory disease and asbestos. *Id.* at 376-81. Ultimately, Manville confirmed a plan of reorganization which, as its cornerstone, established a private asbestos Health Trust to satisfy the claims of all past, present, and future asbestos

the substantive problems addressed in bankruptcy may change over time is to recognize an important truth about the role of the bankruptcy system in its modern form. That is, whether by default or caprice, the institution of bankruptcy has become a medium for relieving the pressure which inevitably builds in a commercial economy for solutions to new and unprecedented societal problems.

Such a system has whatever costs inevitably follow when there is a redistribution of the debtor's assets in bankruptcy. For instance, it may produce the kind of rampant forum shopping that the Collectivists reject as intolerable.[161] However that may be, the urgency of complex problems, newly surfaced and of uncertain conclusion, together with the pressing demands they make for an orderly system to address them, may be sufficiently momentous as to elide all concern over those and other costs. While it is always open to argument whether bankruptcy is the best or most efficient forum in which to respond to any particular problem, its role as a problem-solver in the broad sense has been unequivocally established.[162] Therefore, criticizing an expanded role for bankruptcy, while perhaps warranted on purely theoretical grounds, does not divest it of those expanded functions. It is to an understanding of how bankruptcy serves those functions that our attention and interest is drawn.

Of course, to say that bankruptcy encompasses more than the narrow issue of debt collection is not to say that every problem is or should be a bankruptcy problem. For that matter, certainly not every debt collection problem is best solved in bankruptcy.[163] Drawing these lines involves difficult policy choices. In large measure, it has fallen to the bankruptcy courts to define the new limits on access to bankruptcy relief. If, as we have argued, the parameters of the bankruptcy process are yet to be determined and perhaps are even indeterminable, the courts need an instrumentality to assure controlled expansion or contraction of the fixed body of substantive bankruptcy law to accommodate ever-changing views about what the process should include. Good faith, we suggest, is

health victims. *See In re* Johns-Manville Corp., 68 Bankr. 618 (Bankr. S.D.N.Y. 1986), *aff'd sub nom.* Kane v. Johns-Manville Corp., 843 F.2d 636 (2d Cir. 1988).

161 *See* Jackson, *supra* note 6, at 861-64; Baird, *supra* note 81, at 824-26; *see also supra* notes 101-36 and accompanying text (discussing Baird and Jackson's theory of bankruptcy).

162 This is basically the position Professor Kennedy takes in attempting to justify the use of bankruptcy process to deal with the problems of asbestos producers and environmental polluters. Kennedy, *supra* note 8.

163 Warren, for example, distinguishes between state collection law, which focuses on a single default and the creditor's right against the debtor, and bankruptcy law, which is concerned with multiple defaults and the rights of creditors *inter se*. Warren, *supra* note 82, at 780-82. Accordingly, absent special circumstances, the courts have held that involuntary bankruptcy is inappropriate in a "single creditor" contest because of the availability of state collection procedures. *See, e.g.*, Bankers Trust Co. BT Serv. Co. v. Nordbrock (*In re* Nordbrock), 772 F.2d 397, 399-400 (8th Cir. 1985); S. SNYDER & L. PONOROFF, *supra* note 21, at § 5.07[2][a].

that instrumentality. Implicit in this proposition, of course, is the basic jurisprudential assumption that the courts and the judiciary are the appropriate political agency for making these scope determinations. Since that assumption, while central to the meaning of good faith as we have conceived it, is not shared in all quarters, it warrants further consideration.

For two essential reasons, we believe, the judiciary is the appropriate repository of power to decide issues of bankruptcy's scope.[164] First, the decisions of courts, endlessly memorialized in a continuous stream of published opinions,[165] are subject to both immediate and reflective scru-

---

164 The role of bankruptcy courts in implementing bankruptcy policy is a point of contention between Collectivists and Traditional scholars. Baird and Jackson appear extremely skeptical of the ability of bankruptcy judges to manage competing interests in a manner that will ensure efficient asset deployment. Their skepticism seems to arise principally out of what they regard to be a poor judicial track record in protecting the interests of secured creditors. *See, e.g.*, Baird & Jackson, *supra* note 6, at 126-27. Baird, in his debate with Warren, states:

> Warren relies . . . on the bankruptcy judge to ensure that everything comes out right in the end. But judicial discretion is no panacea . . . . Warren puts too much faith in the ability of bankruptcy judges to control the conflicting incentives of the various parties.
>
> . . .
>
> Jackson and I have no objection to judicial discretion per se.
>
> . . .
>
> Our argument is simply that . . . traditional scholars are too willing to accept the steady hand of a fair judge when other ways of keeping the parties in line may be preferable.

Baird, *supra* note 81, at 820-21. Baird and Jackson also have argued that bankruptcy judges routinely overestimate a firm's prospects for rehabilitation in Chapter 11. *See* Baird & Jackson *supra* note 6, at 126-27. The result is undercompensation to secured creditors. *Id.* at 128-29.

Warren disagrees sharply with Baird and Jackson:

> Bankruptcy judges are impartial decision makers. They balance the competing interests of the parties according to statutory guidelines. Their meat-and-potatoes job is to make decisions about lifting stays, approving plans of reorganization, and the like—decisions requiring an understanding of the interests of the debtor and all the creditors and a willingness to search the statute to follow its distributional scheme.

Warren, *supra* note 82, at 805.

Of more immediate interest here is the role of the courts in the evolution of bankruptcy purposes and policy. A central premise of this Article is that the courts are the principal agency in the evolutionary process. Of course, the Collectivists would deny this role to the courts as a necessary concomitant to the proposition that bankruptcy serves only a single static purpose. This leaves no room for an evolution of purposes to address emerging social and economic exigencies, thereby eliminating the need of an agency to oversee it.

> [T]here is a more important reason for denying a bankruptcy judge broad license to protect people in the wake of economic misfortune. The problems brought by business failures are not bankruptcy problems. A bankruptcy proceeding should not be the place to implement a policy that society does not enforce outside of bankruptcy and that is unrelated to the preservation of assets for the firm's investor group.

Baird & Jackson, *supra* note 6, at 102.

165 We recognize that this assertion is somewhat overstated. Not all judicial decisions are published and available. For discussion and quantification of the extent of unpublished opinions at the U.S. Court of Appeals level, see Richman & Reynolds, *An Evaluation of Limited Publication in the United States Courts of Appeals: The Price of Reform*, 48 U. CHI. L. REV. 573 (1981); Richman & Reynolds, *The Non-Precedential Precedent—Limited Publication and No-Citation Rules in the United States Courts of Appeals*, 78 COLUM. L. REV. 1167 (1978) (suggesting that the phenomenon of unpublished opinions is problematic insofar as the goals of Anglo-American judging are con-

tiny. This presents the opportunity for an indirect discourse to develop between courts and those who critique their efforts through scholarly writing. The scrutiny of scholars provides not only strong incentives for careful decisionmaking, but also affords judges in the trenches an occasional aerial view of the legal landscape.[166] Removed from the daily pressures of deciding individual cases, commentators can observe and bring to the fore trends that might otherwise escape the attention of the decisionmaker.[167] The resultant dialectic minimizes the potential for random or inconsistent decision making.

The second reason that the judiciary is the appropriate entity to regulate bankruptcy access is the very conclusion that the role of the bankruptcy process is continually changing. This critical fact places a premium on an agency which is at once tolerant of a dynamic process and naturally resistant to sweeping and abrupt change. Limited to deciding specific disputes between specific litigants, courts are by and large incapable of implementing change other than at a molecular level. In sharp contrast to a legislative body, which acts broadly, abstractly, and episodically, courts can only react in a relatively measured and incremental fashion. This ensures that the evolution of bankruptcy policy will proceed at a similar pace.

B. The Good Faith Calculus

These principles are strikingly illustrated in the courts' use of the good faith doctrine to analyze issues of bankruptcy access. The term "good faith" has a long and storied history in the law.[168] It is a work-

---

cerned). To the extent the problem of unpublished opinions exists generally in the law, it may be particularly acute in bankruptcy because of the additional numbers of courts and judges rendering bankruptcy decisions. Nevertheless, the widespread publication and availability of bankruptcy judges' opinions under the Code has made the problem less acute than it was under the earlier Bankruptcy Act.

166 The very accessibility of reported cases itself presents a hazard, one that Llewellyn once described as the threat of availability. The threat posed arises from the natural tendency to look first, and, perhaps exclusively, to the most readily available source of data in undertaking any inquiry. The cost is in lost perspective, since, as Llewellyn put it, we might "come shortly to mistake the merely available, the easily seen, for all there is to see." K. LLEWELLYN, JURISPRUDENCE 82-83 (1931). In this connection, it is also worth considering the recent study described in T. SULLIVAN, E. WARREN & J. WESTBROOK, AS WE FORGIVE OUR DEBTORS (1989) (testing a considerable body of standard assumptions about bankruptcy against empirical data). The endeavor is reviewed in *As We Forgive Our Debtors*, 65 IND. L.J. 1-139 (1989) (symposium).

167 *Cf.* Baird & Jackson, *supra* note 6, at 97 n.1 (judges capable of adopting a broad perspective on matters of policy are those "who are not immersed on a daily basis in bankruptcy law.").

168 Good faith in the law has received and continues to receive a good deal of scholarly attention on both theoretical and practical levels. The leading article on the theoretical level is, doubtless, Summers, *"Good Faith" in General Contract Law and the Sales Provisions of the Uniform Commercial Code*, 54 VA. L. REV. 195 (1968). Summers argues that good faith is a term without affirmative substantive content of its own but finds meaning only in exposing and disapproving instances of bad faith. It is, to use Summers's term, an "excluder." *Id.* at 196. According to Summers, the lawyer does not ask what a judge means by good faith in a case, but asks "[w]hat, in the actual or hypotheti-

horse in the legal vocabulary and a directive that has been woven into the very fabric of Anglo-American law and jurisprudence. Good faith has been called upon in radically disparate contexts to establish the outer boundaries of acceptable behavior.[169] Perhaps for this reason, if the phrase "good faith" ever had a single meaning of its own, it has long since been lost in the course of expanded and expanding applications of the doctrine.[170] Indeed, in large part, the term "good faith" has become

---

cal situation, does the judge intend to rule out by his use of this phrase? Once the relevant forum of bad faith is thus identified, the lawyer may assign a specific meaning to good faith by formulating an 'opposite'." *Id.* at 200 (footnotes omitted).

Summers's excluder analysis has been criticized. *See, e.g.*, Burton, *More on Good Faith Performance of a Contract: A Reply to Professor Summers*, 69 IOWA L. REV. 497 (1984); Patterson, *Wittgenstein and the Code: A Theory of Good Faith Performance and Enforcement Under Article 9*, 137 U. PA. L. REV. 335 (1988). Patterson's article, which is commended to the reader on grounds of general interest, rejects excluder analysis as offering little or no guidance for predicting whether an actor's behavior will be regarded as amounting to good faith or bad faith: "The logic of the excluder analysis leads to the unacceptable conclusion that only cases with extremely similar fact patterns have value as precedent." *Id.* at 351 (footnote omitted).

Beyond suggesting the shortcomings of the excluder analysis, Patterson's article proposes a purposive approach to conceptualizing good faith based mainly on the work of Wittgenstein. *Id.* at 342. The approach proceeds from the emminently sensible idea that we can best learn what good faith means by considering the purposes the doctrine serves in legal discourse. *Id.* at 370-71. The theory also is noteworthy for its intelligent perspective on the role of historical or original intent in assigning meaning to concepts such as good faith. Its author grants "institutional history" a respectable place in analysis, but insists on revising the meaning that history would import "along nonsubjective . . . lines when the context and textual materials so indicate." *Id.* at 390. Finally, and of immediate concern here, the purposive approach admits the prospect of the evolution of concepts such as good faith. *Id.* at 425.

169 A brief review of the recent literature reveals the broad range of applications. *See, e.g.*, Burkoff, *Bad Faith Searches*, 57 N.Y.U. L. REV. 70, 71 (1982) (discussing whether a searching officer's bad faith renders an otherwise constitutional search unconstitutional); DeMott, *Puzzles and Parables: Defining Good Faith in the MBO Context*, 25 WAKE FOREST L. REV. 15 (1990) (discussing the role of good faith in buyout transactions); Note, *Damage Measurements for Bad Faith Breach of Contract: An Economic Analysis*, 39 STAN. L. REV. 161, 162-63 (1986) (a critique of the economic efficiency of tort damages in bad faith breach of contract actions); Note, *Extending the Bad Faith Tort Doctrine to General Contracts*, 65 B.U.L. REV. 355 (1985) (discussing the tort of bad faith, its history, and recent trends); Note, *"Contort": Tortious Breach of the Implied Covenant of Good Faith and Fair Dealing in Noninsurance, Commercial Contracts—Its Existence and Desirability*, 60 NOTRE DAME L. REV. 510, 525-26 (1985) (criticizing the expansion of the bad faith cause of action beyond the context of insurance contracts).

In commercial law, the duty of good faith is directly imposed by the Uniform Commercial Code, *see* U.C.C. §§ 1-203, 2-103(1)(b), and by the *Restatement*, *see* RESTATEMENT (SECOND) OF CONTRACTS § 205 (1981). Articles dealing with the good faith obligation at various stages of contract negotiation, formation and performance are collected in Burton, *Breach of Contract and the Common Law Duty to Perform in Good Faith*, 94 HARV. L. REV. 369, 369-70 n.5 (1980). Among other excellent articles discussing good faith in commercial law are Farnsworth, *supra* note 43; Gilmore, *The Commercial Doctrine of Good Faith Purchase*, 63 YALE L.J. 1057 (1954).

170 Good faith is relevant in a variety of bankruptcy contexts. In addition to the implied obligation to file in good faith, good faith is requisite to confirmation of a plan in Chapter 11 under § 1129(a)(3) of the Bankruptcy Code, and in Chapter 13 under § 1325(a)(3). To earn court approval, reaffirmation agreements under § 524(c) must have been entered into in good faith. For an excellent survey of these and other applications of good faith in the context of the bankruptcy pro-

little more than a convenient way to refer to a set of criteria by which conduct is tested.[171] At the same time, the term continues to evoke an immediate and shared understanding that the actor's subjective honesty has been called into question.[172] Whatever the problem the good faith doctrine has been requisitioned to resolve, the one constant has been this murky but persistent idea of a moral imperative.

The malleability of the doctrine, the result of a rich history of varied applications, together with its capacity to call to mind certain familiar referents of honesty and dishonesty, make good faith a singularly useful instrument to aid the development of the contours of the bankruptcy process. Application of an implied good faith requirement in bankruptcy thus functions less as a substantive rule of standing or eligibility to file,[173] and more as an enabling convention allowing the bankruptcy courts to systematically test their performance in guarding the portal into bankruptcy. In other words, a good faith filing requirement is inevitable once it is acknowledged that the system accommodates an evolving reality of social, political, and economic challenges. Good faith, through its ability to evoke sympathetic signification, not only provides the framework for meaningful discussion, but assures that the evolution of the law is the product of a studied and temperate effort rather than the consequence of a series of aimless and unconnected fits and starts.

How have courts employed the good faith doctrine to permit well-considered, conscientious expansions of the ends of the bankruptcy process? Initially, it is important to recognize that cases have not begun with a good faith doctrine fully developed for the task. Instead, as the instrument of a controlled evolution, the doctrine is no more fixed than the process it seeks to steer. Good faith evolves alongside the process

---

cess, see Ordin, *supra* note 11; *see also supra* note 68 (discussing bad faith in connection with the filing of involuntary petitions) & note 69 (discussing bad faith in connection with the confirmation of debt adjustment plans under Chapter 13).

171 *See infra* text accompanying notes 178-79.

172 For example, this mainly subjective feature of good faith finds expression as "honesty in fact," *see* U.C.C. § 1-203, and as "decency, fairness or reasonableness," *see* RESTATEMENT (SECOND) OF CONTRACTS § 205, comment a (1981). If the good faith doctrine is flexible as we have indicated, *cf.* DeMott, *supra* note 169, at 19 (discussing plasticity of the good faith doctrine in the context of judicial review of transactions calling for the exercise of ordinary business judgment), its specific features will vary according to the legal context in which the doctrine operates. Purposive, context-sensitive interpretation of the term does not of necessity preclude the existence of a constant, broadly understood referent, such as the subjective moral component that recurs in various applications of the doctrine. *See generally* Patterson, *supra* note 168 (reconceptualizing good faith in accordance with the purposive principles of interpretation, but rejecting Summers's position that the term is empty of positive content). Thus, good faith may remain relatively formless yet enjoy positive content. Coupled with the doctrine's malleability, this enduring, if vague, positive content has made good faith the useful device it has become.

173 We believe that it would be unduly restrictive to view the implied good faith requirement in the same light as the statutory eligibility rules in 11 U.S.C. § 109 (1988). *See supra* note 7.

itself as it is brought to bear on questions of the appropriateness of particular cases in bankruptcy.

We believe, however, that it is possible by studying the cases to understand a great deal about the evolutionary process. The cases not only enable us to identify and critique the present contours of bankruptcy policy, but they also suggest the normative inclinations which might be expected to influence the outcome of future decisions—decisions that will play a significant part in shaping the contours of future bankruptcy policy.[174]

On assembling the good faith cases into the three loose categories we earlier suggested,[175] we were at once struck by an easily observable pattern: one-asset/one-creditor cases are frequently dismissed for want of good faith; the public company filing is never dismissed on bad faith grounds; and filings by economically viable companies making tactical use of the bankruptcy system are occasionally dismissed on this basis.[176] Alone, these results do not tell us much about the direction of bankruptcy policy. For instance, we could easily hypothesize a reorganization case filed by a large, sophisticated "Fortune 500" company that might be no more appropriate for bankruptcy relief than a "new debtor syndrome" case.[177] Yet, despite the surge in public company filings in recent years, the case law fails to provide us with a single example to date. Why not? The process and results of categorizing decided cases, by definition, cannot answer that question. Organizing the cases into these broad, descriptive groups is useful only insofar as it facilitates the next level of analysis; and, in fact, excessive commitment to such groupings inevitably will produce the wrong result when a difficult case presents itself for consideration. Once hewn, such classifications can foster a nearly irresistible urge to decide new cases based entirely upon the predetermined categories into which they fall. Yet, if good faith cases exist only by dint of previously decided disputes, then past decisions serve merely to highlight the flow and development of bankruptcy policy; they do not forever establish its boundaries. Therefore, it is important to go

---

174 Oliver Wendell Holmes once opined,

> If you want to know the law and nothing else, you must look at it as a bad man, who cares only for the material consequences which such knowledge enables him to predict, not as a good one, who finds his reasons for conduct, whether inside the law or outside of it, in the vaguer sanctions of conscience.

O. W. HOLMES, *The Path of The Law*, in COLLECTED LEGAL PAPERS, at 171 (1920). It is our hope here that in the effort to "know the law" concerning the implied obligation of good faith, we may gain a sense of the "vaguer sanctions of conscience" that have given rise to the judiciary's normative political position on the purposes and policy of bankruptcy.

175 *See supra* text accompanying note 27.

176 *See supra* note 69 and accompanying text (discussion on the criteria generally regarded as determinative in resolving good faith challenges in the litigation tactic cases).

177 *See infra* notes 224-40 and accompanying text (analyzing an attack on good faith in the Texaco filing which, we believe, might have been successful under the conditions hypothesized).

beyond mechanical division of the cases in favor of a more demanding and policy-sensitive analysis.

For this reason, in the second part of our analysis, we move closer to the individual cases within the categories to discover that frequently the articulated ground for decision is not revealing. For example, in examining the cases in the one-asset debtor category, we found little more than the simple logging of criteria or factors routinely, if solemnly, recited by the courts as badges of bad faith.[178] Moreover, the relative value of these criteria seems to shift from case to case and even within cases,[179] making it impossible to derive or fix a single linear relationship among the criteria or to assume that nothing more than a straightforward balancing of those factors is being undertaken.

Similarly, cases like *Continental Airlines*[180] and *Manville*[181] mostly contain bland declarations to the effect that so long as the debtor appears capable of successfully reorganizing its enterprise, allegations of improper motive will be given little weight. Standing alone, that proposition might be considered an innocuous one, but it is hardly consonant with the abuse of process theme that pervades discussion of the good faith question in one-asset debtor cases.[182] The problem with these declarations, at least when taken at face value, is that they evade or, at best, only obliquely respond to the truly significant question raised by a good faith challenge—namely, what are currently the central purposes to be served by the bankruptcy process? To discover the determinants actually at work in these decisions, we must go beyond the casual and, not infrequently, inconsistent declarations upon which the decisions purport to rest. When we abandon the attempt to rationalize a case solely in terms of a menu of criteria having independent significance, we are free to reorganize these criteria and other factors relied on by the courts around certain basic considerations of policy and purpose.

In keeping with our thesis that bankruptcy policy continually evolves, principally at the hands of courts employing the mediating device of good faith, our analysis dictates that we return to the case law to identify the broad, recurring themes that delineate the evolutionary process. Careful explication of the cases is rewarded with a clearer idea of the current state of that evolution and likewise casts light upon its future direction. It is important, however, to disclose the limits of an analytical

178 *See supra* note 39.

179 That they do so is not to suggest disingenuousness in the decisionmaking process. In fact, in Carolin Corporation v. Miller, 886 F.2d 693 (4th Cir. 1989), the court openly acknowledged that "no generally accepted proof requirements have emerged," and "there is no 'single factor that will necessarily lead to a finding of bad faith' " in every case. *Id.* at 701 (quoting Natural Land Corp. v. Baker Farms, Inc. (*In re* Natural Land Corp.), 825 F.2d 296, 298 (11th Cir. 1987)).

180 38 Bankr. 67 (Bankr. S.D. Tex. 1984), discussed *supra* notes 45-48 and accompanying text.

181 36 Bankr. 727 (Bankr. S.D.N.Y.), *appeal denied*, 42 Bankr. 651 (S.D.N.Y.), *reh'g denied*, 42 Bankr. 654 (S.D.N.Y. 1984), discussed *supra* notes 49-57 and accompanying text.

182 *See supra* notes 29-36 & 43-44 and accompanying text.

approach, such as ours, that derives largely from positive law. Since propositions abstracted from cases can no more be expected to conform to any logical ideal than the cases from which they proceed, it would be nonsense to suppose that the derivative propositions themselves reflect a unified system capable of formulaic expression in absolute terms. Our end, therefore, is to propose a calculus, not an equation.

As observed earlier, the courts, particularly in the one-asset debtor cases, are inclined to articulate and then apply a laundry list of illuminating factors to decide whether a filing was undertaken in good faith.[183] Our study and synthesis of the cases leads us to believe, however, that there is more at work here than the mere juggling and reconstitution of those factors. We discern in this exercise an unexpressed intermediate step in the process that is apparent only with the recognition that the so-called factors or indicia of good faith are not actually themselves proof of good or bad faith; rather, they serve to identify a category or type of case which has been earmarked by courts as suspect. What type of case is suspect? In our view, it is the case that manifestly fails to present the pattern which everyone, Collectivists and Traditionalists alike, agrees invokes the core function of bankruptcy—namely, to resolve the problem of multiple defaults and limited assets.[184] Once identified, the suspect case is isolated for closer scrutiny to determine its concordance with current bankruptcy policy. In the final analysis, it is the result of that strict scrutiny which determines good faith or bad faith, and explains why not all one-asset debtor cases are dismissed for want of good faith.[185]

A case may also be identified as suspect when, from the surrounding circumstances, it can reasonably be inferred that the filing, voluntary or involuntary, was precipitated by an exigency other than the problem of multiple defaults. For instance, that the debtor's primary desideratum was to obtain leverage in a pending civil contest or a permanent advantage in labor relations, rather than to stave off impending financial collapse, has been considered grounds for suspicion.[186] Like the one-asset debtor situation, this kind of case has been singled out for closer scrutiny because of its apparent factual remoteness from the prototypical bankruptcy case. However, if one believes, as we do, that bankruptcy has

---

183 *See supra* note 39 and accompanying text.

184 For discussions of the Collectivist and Traditional views of bankruptcy, see *supra* notes 90-93 & 126-28 and accompanying text.

185 *See supra* notes 41-43 for citation of cases generally filling the one-asset debtor description that nevertheless were allowed to proceed.

186 The latter charge has been levelled in particular against airline filings, including, most recently, Eastern Airlines. *See supra* note 59 and accompanying text; *infra* notes 212-13 and accompanying text; *see also* Note, *American Airlines Discover Chapter 11: Is it Reorganization or Union Busting?*, 11 J. CONTEMP. L. 375 (1984) (discussing the debate over airlines' use of Chapter 11 to circumvent labor contracts). For an exhaustive treatment of the interaction and conflict between federal bankruptcy law and federal labor law, see West, *Life After* Bildisco: *Section 1113 and the Duty to Bargain in Good Faith*, 47 OHIO ST. L.J. 65 (1986).

come to serve functions in the legal system beyond resolving the common pool problem, this identification of the case marks only the beginning point for inquiry.

From our reading of the cases, then, we infer a two-step analysis at work beneath the routine discussion of motive, badges of bad faith, and ability to reorganize. The first step, again, is identification of the case as suspect. The second step involves a calculus that can be expressed in terms of two pivotal considerations, which we have termed intent and impact. Although simple in its formulation, this calculus can become quite complex in operation due to the varying attention these two considerations receive from one case to the next.

Preliminarily, it is necessary to give substantive content to the terms "intent" and "impact" for our purposes. The courts that address the implied good faith filing issue frequently speak in terms of intent.[187] In that context, we believe intent most often means the sum of the motives inferred from objective facts that prompted the filing.[188]

Every filing, we believe, is a product of an admixture of motivations.

---

187 What is confusing in the case law, however, is that the intent element has been phrased in a variety of different ways, such as intent to rehabilitate, intent to reorganize, intent to conduct business, intent to harass and delay creditors, honest intent, intent to cause malicious injury, and so on. *See generally* authorities cited *supra* notes 33 & 43. We think analysis would be facilitated if all these expressions of the intent consideration were reduced to a single referent. Thus, we have tried to deduce from the cases a more precise sense of what concerns courts have in common when they speak of the debtor's intent. As discussed *infra* note 189 and accompanying text, we have concluded that these concerns all revolve around the objectives which the debtor (or petitioning creditors in an involuntary case) seeks to accomplish by invoking the bankruptcy process.

188 We recognize that in several bodies of substantive law intent and motive are accorded particular meaning and are technically treated differently from one another. For example, in substantive criminal law, motive is defined as the emotional urge or desire which prompts an action, while intention is viewed as the immediate effect to be obtained by committing a particular act. Thus, the the criminal actor intends the crime that is necessary to satisfy her ultimate, underlying desire. In their widely regarded treatise on criminal law, LaFave and Scott use the following example to illustrate the distinction: "[W]hen *A* breaks into *B*'s house in order to get money to pay his debts, it is appropriate to characterize the purpose of taking money as the intent and the desire to pay his debts as the motive." W. LAFAVE & A. SCOTT, JR., CRIMINAL LAW § 3.6(a), at 228 (2d ed. 1988); *see also* W. KEETON & D. DOBBS, PROSSER AND KEETON ON THE LAW OF TORTS ch. 2, § 8 (5th ed. 1984).

We obviously use the term "intent" in a more expansive sense than described above. We subsume within the concept a multiple of variables which relate not only to a debtor's immediate purpose (*i.e.*, intent technically defined), but also to the debtor's ultimate ends and objectives (*i.e.*, motive technically defined). Thus, it matters to us not only that the debtor wants the immediate benefit of the automatic stay, but why. This allows us to relate intent in any particular case (which may be the product of a number of different motives) to core bankruptcy purpose. *See supra* text accompanying note 33.

Since true state of mind is known only to the actor, a phenomenon complicated when the actor is a reified being such as a corporation, purpose can only be gleaned from contextual circumstances. Thus, it is the very facts that warn of suspect intent in the first instance (*e.g.*, one-asset and no unsecured creditors) from which, upon close inspection, the court deduces the intent or lack of intent to rehabilitate a failing business.

Where it is evident that the dominant motive is debt collection relief in the traditional sense of adjusting the rights of multiple claimants, courts have had little trouble concluding that the case before them belongs in bankruptcy, based on the intent consideration alone. The more complex the debtor's organizational structure, however, and the more complicated its financial affairs, the more difficult and less meaningful it becomes to talk about subjective motivation. Ultimately, in a sophisticated or large public company case where a multitude of impulses could have inspired the filing, courts are thoroughly confounded in their effort to isolate a primary or preeminent motive. In these instances, the appropriateness of the case for bankruptcy turns largely on what we call impact. In any given case, impact takes into account: (1) the size of the community affected by the debtor's filing, which frequently is a function of the size of the debtor enterprise; (2) the immediacy of the effects of the filing upon that community; and (3) whether the particular adversities that prompted the filing are adequately addressed elsewhere.[189]

With these definitions of intent and impact in mind, we turn our attention to their interaction since it is that interaction which forms the basis for determining bankruptcy purposes. Earlier, we noted that courts weigh the two considerations differently depending on the case. From this, we conclude that the relationship between intent and impact is one of interactive and mutual dependence. Consequently, the relationship can easily be described and understood with the help of a Cartesian graph, the axes of which are established by our two elemental considerations.[190]

The intent consideration is plotted along the vertical or "Y" axis. At the base of this axis we find the case where there is a complete correspondence of the filer's intent with the historic and still foundational function of bankruptcy.[191] For the sake of convenience, we refer to this point as "orthodox intent." At the apex of the axis is the case having no correspondence of intention with that historic function, what we refer to as "unorthodox intent." This case represents the filing with none of the

[189] *See generally supra* notes 135-40 and accompanying text. This aspect of the calculus runs afoul of Collectivist thought limiting bankruptcy to a single purpose. *See* Baird & Jackson, *supra* note 6, at 103 ("Other problems should be addressed as general problems, not as bankruptcy problems. Social reform should be brought about through broad changes in the substantive law rather than through ad hoc modifications of rights in bankruptcy."); *see also supra* note 164 (discussing the effects of limiting bankruptcy to a single purpose and the role of bankruptcy courts).

[190] Again, we propose a calculus to focus our interpretative efforts, not a formula that would lead unerringly to absolute answers in particular cases. The calculus is not offered to supplant careful analysis, but to facilitate it. It also bears repeating that the calculus is not intended to declare whether a case is appropriate for bankruptcy as a matter of normative policy. It is one thing to aver that a heuristic explains and predicts results in cases, and quite another to say it tells us what the outcomes *should* be in those cases. Of course, a purely descriptive model is useful in evaluating cases because it focuses attention on those cases having arresting dissimilarity from those that suggested the model. Such cases might then become the subject of normative critique.

[191] *See supra* notes 89-93 and accompanying text.

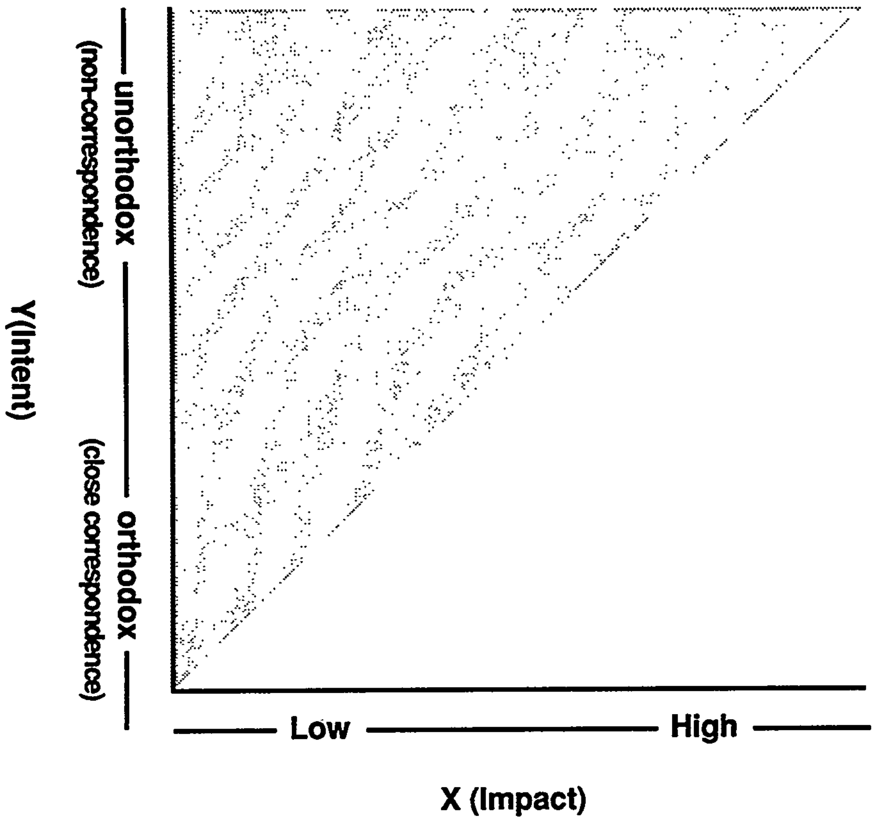

Fig. 1

characteristics of cases presenting the archetype common pool problem.[192]

The impact consideration is plotted along the horizontal or "X" axis. At the point where the "X" axis intersects the "Y" axis is the case of least impact. The farther one proceeds along the "X" axis away from that intersection, the greater the impact of the case.

Drawing a line at a 45-degree angle from the intersection of the "X" and "Y" axes illustrates the relationship we believe exists between the intent and impact variables. Cases plotted into the shaded area of the graph on the basis of the good faith calculus would be subject to dismissal. Conversely, cases plotted into the unshaded area of the graph would survive a threshold good faith challenge.

---

192 *See supra* notes 90-93 and accompanying text.

It bears reiterating at this point that what we hope to display by use of this graph are the boundaries that currently circumscribe the permissible scope of bankruptcy. This is a very different exercise from attempting to define the borders of good faith. Analysis of the subject to date has sometimes floundered because of the failure to recognize this distinction.[193] In our analysis, the object is not to define good faith, an exercise without purpose once the concept of good faith is recognized to be nothing more than the instrumentality used by the courts to control the evolution of the bankruptcy process. Instead, we consider it important to talk about good faith only insofar as it facilitates discussion of the unfolding of bankruptcy policy.[194]

C. *The Good Faith Cases Reconsidered*

Having elaborated an abstract, analytical calculus, we arrive at the point of its concrete application. We begin by returning to the cases discussed and categorized in Part I of this Article to illustrate how specific filings might be plotted along the impact and intent axes. We conclude by making some predictions based on the application of the calculus under hypothetical conditions which we believe might bear some similarity to future cases in which the good faith filing requirement could be profitably invoked.

In giving content and dimension to the good faith calculus, it is helpful to begin with the one-asset debtor case which, it will be recalled, is most often characterized by the recent transfer of encumbered property to a newly created debtor lacking those features ordinarily associated with regular business operations.[195] On their face, these primary facts indicate an intent so remote from orthodox intent and a level of impact so idiosyncratic as to make the one-asset debtor case the prototype for dismissal on bad faith grounds. Accordingly, the one-asset debtor case establishes points along the impact and intent axes amount-

193 *See, e.g.*, Cohn, *supra* note 11. Cohn's article, in general a good discussion of the one-asset debtor case, struggles unsuccessfully to find an operative, unifying theme from among the lists of bad faith indicia that characterize the opinions in those cases. Cohn is unable to proceed much beyond this point because he treats the finding that a petition was filed for an *outré* purpose as merely one among the indicia or factors on the list. When analysis proceeds from that basis, it invariably must deteriorate to tautology since, as Cohn correctly notes, to state that a case should be dismissed because it was filed for the wrong purpose begs the question. *See id.* at 142. Cohn ultimately is forced to conclude that the attention given by courts to factors suggesting good or bad faith is digressive and that their time would be better spent in deciding whether or not the purpose of the filing is a correct purpose. This misapprehends, in our judgment, both the role of good faith and the meaning of the discussion in the cases devoted to the purpose of the filing. The badges of bad faith become meaningful only when they are understood to be the means of inquiring into the evolving purposes of bankruptcy rather than the end objects of the good faith inquiry.

194 *See supra* notes 168-73 and accompanying text. This instrumental approach to the good faith filing requirement, we believe, differentiates our approach from the approaches of others to date.

195 *See supra* notes 29-35 and accompanying text.

ing to the current reported extremes of low impact and unorthodox intent alike.

In the one-asset debtor case fitting the prototype pattern, the discernible impact, direct or otherwise, is restricted to a single creditor. No other interests are measurably implicated by the filing. The situation presents nothing more than a collection problem between the debtor and a single creditor, and an adequate state debt collection system exists to advance that collection process while protecting the rights of both parties.[196] If, as we have argued, good faith regulates improper uses of the process,[197] then it is easy to understand why most of the cases dismissed on this ground have fit the one-asset debtor scenario in its classic form. When the debtor defaults on its obligations to the secured creditor and then files for Chapter 11 relief on the eve of foreclosure, the abuse is obvious because the facts from which it is inferred are simple. The debtor has no intention to reorganize, and probably could not successfully do so in any case. The filing is a stalling tactic designed to upset regularized, well-accepted state law debt collection processes constructed with precisely this situation in mind. The net social and economic loss resulting from the demise of such a debtor is negligible.

On the other hand, it is important to keep in mind that merely to identify a case as belonging in the one-asset debtor category is not to identify it as a prototype case for dismissal. That is, the act of classifying the case is not dispositive of the good faith issue should it be raised by creditor motion or by the court on its own initiative.[198] As a practical matter, courts decide that close scrutiny of a case is in order when, for instance, either the debtor owns limited assets acquired by recent transfer or is not actively engaged in the operation of a business.[199] The burden then falls to the debtor, in light of all of the facts, to divorce its case from the prototypical one-asset debtor case to survive the motion. The fewer category-defining criteria a debtor shares with the prototypical case, the more orthodox its intent and the greater the overall impact of the filing. At some point, a debtor will succeed in moving sufficiently along the intent axis, the impact axis or both so as to avoid dismissal. This movement of an actual case away from the unorthodox intent/low impact extreme is illustrated by the broken line drawn between two points on the graph. Point "a" represents the prototypical case for dismissal, and point "b" represents the one-asset debtor case closest on its facts to the prototype which has been permitted to proceed in spite of early challenge

196 *See supra* note 163.

197 *See supra* note 74 and accompanying text.

198 As we earlier noted, grouping the cases into categories is the beginning point of analysis, not the terminus. *See supra* text accompanying notes 31-33.

199 These are the impressionistic facts which create at the threshold a suspicion about the propriety of the case for bankruptcy. *See supra* note 186.

on grounds of bad faith.[200]

In the case of a large public company filing, it is usually the ability

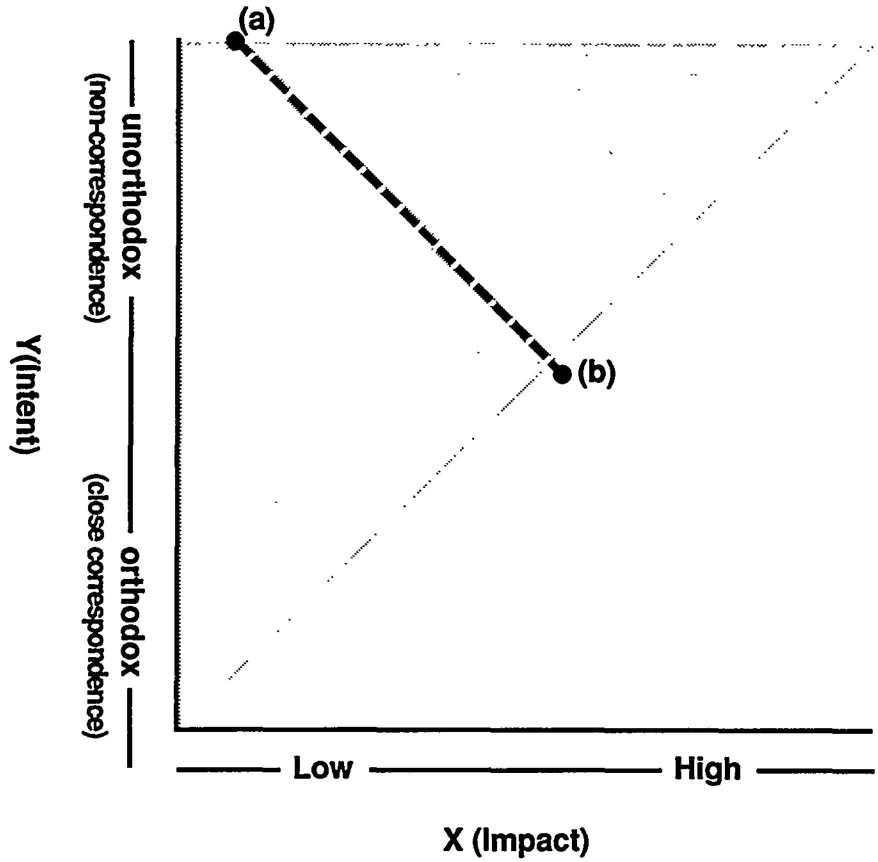

Fig. 2

to derive strategic advantages in bankruptcy not available outside of a Chapter 11 proceeding which invites good faith challenges.[201] In these cases, the preliminary inquiry into the debtor's intent (as we use that term) will almost always lead to close scrutiny for two reasons. First, the infrastructure that forms the operating framework of the large debtor

200 Since the factors influencing movement on both axes are related (*i.e.*, higher impact corresponds with more orthodox intent and vice versa) the line illustrating the movement of one-asset cases away from the prototype case can be expected to appear at a 45-degree angle inverse to the 45-degree angle line which separates good faith cases from bad faith cases.

201 *See supra* text accompanying notes 45-48.

enterprise is nearly always complex and extensive, having the potential to spawn a dizzying array of motivational impulses. This results in uncertainty as to the significance to attach to any particular motive, thereby warranting close systematic attention to the issue of intent.

Second, resolution of the intent question is complicated by the fact that in the mega-reorganization case there is seldom a clear answer to the question whether the case presents a common pool problem. This uncertainty is a product of the subjectivity and arbitrariness that attend the process of applying so-called generally accepted accounting principles to large, multi-dimensional enterprises.[202] It is infinitely more difficult to identify and weigh a motivation to solve a common pool problem when there is considerable doubt as to whether such a problem even exists.

For the two reasons stated above, courts are likely to have difficulty in determining the existence of orthodox intent. Thus, we believe the next step, which involves the balancing of intent and impact, will almost invariably be taken, if only implicitly, in the large reorganization case. However, the impact quotient in the public company reorganization is frequently so enormous that it can be expected in most cases to carry the day for the debtor.[203] Certainly this is the teaching of the *Continental Airlines*[204] and *Manville*[205] decisions. We have no particular quibble with the result in either case, although, because of the well-developed body of federal law in place to respond to and control most labor management disputes,[206] we see *Continental Airlines* as the closer of the two calls. Yet, even if the impact quotient was not as great in that case (because of the adequacy of an extant body of governing non-bankruptcy

---

202 *See supra* note 53 and accompanying text.

203 *See supra* text accompanying note 189. Our definition of impact results from a composite of variable factors, the consideration and balancing of which leads to findings of impact ranging along a spectrum from low to high. We speculate that in the mega-reorganization case, all the factors are likely to be implicated significantly. For instance, the failure of a major enterprise frequently will have profound, immediate economic effects upon the community in which the firm is situated. Employment, local creditors, parasitic service industries, and the like generally will all be affected. Under these circumstances, the fate of a failing enterprise at the local level seems so nearly indistinguishable from that of the community to render thoughts of an effective, prearranged institutional response fanciful.

In other words, in such cases, the effects of massive enterprise failure may prove at once profound, immediate, and without a meaningful palliative. Of course, this is not to say that the failure of modest businesses cannot have great impact or that all mega-reorganizations invariably do.

204 38 Bankr. 67 (Bankr. S.D. Tex. 1984), discussed *supra* notes 45-48 and accompanying text.

205 36 Bankr. 727 (Bankr. S.D.N.Y.), *appeal denied*, 42 Bankr. 651 (S.D.N.Y.), *reh'g denied*, 42 Bankr. 654 (S.D.N.Y. 1984), discussed *supra* text accompanying notes 49-57.

206 *See generally* Countryman, *supra* note 48, at 175 (suggesting that the Continental Airlines filing had opened the floodgates for any company experiencing financial stress to improperly circumvent established labor policy by dropping into bankruptcy court); West, *supra* note 186, at 161 (arguing that in adopting Code § 1113 in the aftermath of the *Bildisco* decision, *see supra* note 5, Congress had unduly favored bankruptcy principles over labor principles in resolving the conflicts between the two areas of law).

law),[207] the immediacy of the company's financial problems, at least as they were found to exist by the bankruptcy court,[208] suggests a better score on the intent scale for Continental than for Manville.

The same reasoning, of course, would seem to make the Eastern Airlines filing[209] less defensible. Like that of its sister company, Continental Airlines, Eastern's filing was precipitated by labor relations difficulties.[210] Moreover, its eventual liquidation nothwithstanding, it is far less clear that Eastern's financial problems in 1989 were as extreme or extensive as those facing Continental in 1983.[211] Nevertheless, since the good faith issue was never formally raised or decided in the Eastern Airlines Chapter 11 case, we must admit that the absence of specific findings regarding the extent and, in particular, the causes of that company's financial distress renders our judgment little more than surmise.[212]

In contrast to the doubts about Eastern raised by our analysis, our good faith calculus strongly suggests that reorganization filings by companies that have been either the facilitators or objects of corporate takeovers should, absent other uniquely mitigating facts, survive attacks on

207 West, *supra* note 186, at 161.

208 *See supra* notes 47-48 and accompanying text.

209 *See supra* note 59.

210 *See generally Advantage, Lorenzo*, BUS. WK., July 10, 1989, at 24; *Going for Broke: Bankruptcy Strategy For Eastern Airlines Could Fail Lorenzo*, Wall St. J., March 10, 1989, at 1, col. 6 (detailing the parallels between the Eastern and Continental cases).

211 While, as a consequence of a strike by the International Association of Machinists Union, Eastern purportedly was losing $1 million dollars a day at the time of its filing, the union and others maintained that the company had provoked the strike so that it could hire non-union workers without violating any contracts. *See* Rodriguez, *Frank Lorenzo's Bench Strength*, LEGAL TIMES, Jan. 8, 1990, at 15, col. 1 (quoting Charles Bryan, president of the Machinists' local). In addition, in connection with their request for appointment of a trustee, the Airline Pilot's Association (which had struck in sympathy with the Machinists union) charged that before filing, Eastern had engaged in numerous intercompany asset transfers which reduced Eastern's net worth by over $100 million. *See Pilots Assert Eastern Transferred Airport Slots Before Bankruptcy*, N.Y. Times, Mar. 17, 1989, at A19, col. 5; *Bankruptcy to Test Union Solidarity*, The Christian Science Monitor, Mar. 13, 1989, at 8, col. 1.

212 In discussing the strategic use of bankruptcy law to accomplish labor relations objectives, Professor Martha West has argued that the Eastern Airlines filing established a new highwater mark. Specifically, she notes that, unlike earlier cases in which the employer was charged with seeking to evade its collective bargaining duties, in Eastern *both* the company and the union seemed to be using the bankruptcy forum to achieve objectives that would not be possible under labor law. *See* West, The Eastern Airlines Strike: Legal Implications (paper prepared for presentation at the Industrial Relations Research Association (IRRA) Annual Meeting, Dec. 1989, and for publication in the IRRA Annual Proceedings) (on file at the office of the *Northwestern University Law Review*).

The very recent decision to liquidate Eastern, and the re-entry of Continental into Chapter 11, may cast further doubt on this suspicion. However, it is exceedingly difficult to gauge how much Eastern, as debtor-in-possession, was hurt economically by the general downturn in the airline industry between the date of its filing and the date the plan to rehabilitate was abandoned. As the new filings by Pan American World Airways and its affiliates attest, the late 1980s were not the best of times to be making a go of it in the airline business, whether in Chapter 11 or not. *See generally Bankruptcy Petition is Filed by Pan Am to Get New Loans*, N.Y. Times, Jan. 9, 1991, at A1, col. 6; *Pan Am Corp. Files for Bankruptcy Protection*, S.F. Chronicle, Jan. 9, 1991, at A1.

good faith grounds.[213] This conclusion follows, first, from the broad disagreement and uncertainty over the economic utility and social impact of hostile takeovers and leveraged buyouts;[214] and, second, from the unprecedented explosion during the 1980s of unsolicited corporate takeovers and the consequent economic fallout.[215] In other words, unless and until alternate mechanisms for dealing with this fallout are established, the bankruptcy system becomes by default the forum where many of the public policy issues surrounding the takeover phenomenon are debated and resolved.

Of all the cases discussed so far, the bankruptcy filing of Texaco, Inc. presents the most serious question of whether a major business filing was a proper use of Chapter 11.[216] Parenthetically, we note that discussion of Texaco's reorganization proceeding also presents the occasion to apply our analysis to the third type of good faith case, the tactical filing.

---

213 A major issue of current interest in bankruptcy is whether or not leveraged buyout transactions are subject to attack as fraudulent transfers in the event of the company's subsequent bankruptcy filing. *See generally* S. SNYDER & L. PONOROFF, *supra* note 21, at § 10.08[8].

214 The literature regarding this subject is prodigious and growing. Some observers have urged a free and unregulated market for corporate control. These commentators principally have based their arguments on the economic theory that hostile takeovers create wealth and serve an important function in disciplining managers of publicly traded companies. *See, e.g.*, ECONOMIC REPORT OF THE PRESIDENT ch. 6 (1985); Jensen & Ruback, *The Market for Corporate Control: The Scientific Evidence*, 11 J. FIN. ECON. 5 (1983); *cf.* Coffee, *Regulating The Market for Corporate Control: A Critical Assessment of The Tender Offer's Role in Corporate Governance*, 84 COLUM. L. REV. 1145 (1984) (admitting the evidence suggesting a managerial discipline value, but proposing alternate explanations of such evidence and raising concern over the more intangible costs of takeovers).

The economic evidence in support of the benefits of hostile takeovers has been challenged on its own terms. *See, e.g.*, Herman & Lowenstein, *The Efficiency Effects of Hostile Takeovers: An Empirical Study*, in KNIGHTS, RAIDERS AND TARGETS 211 (J. Coffee, L. Lowenstein & S. Rose-Ackerman eds. 1988); Leroy, *Efficiency and The Variability of Asset Prices*, 74 AM. ECON. REV. 183 (1984); *see also* Bebchuk, *Towards Undistorted Choice and Equal Treatment in Corporate Takeovers*, 98 HARV. L. REV. 1693 (1985) (arguing that the coercive nature of tender offers may cause shareholders to accept an offeror's bid of considerably less than full value). A number of commentators also have raised concerns over the costs which the threat of corporate takeovers creates in terms of diverting managerial attention away from the long-term interests of the company in favor of short-term rewards to keep investors satisfied. Equally, the dangers of massive conversion of corporate equity to debt, and the effects of takeovers on employees, communities, and other non-shareholder interests, have been offered as additional justification for greater regulation and control of takeovers in the interest of the national economy at large. *See generally* Proxmire, *What's Right and Wrong About Hostile Takeovers?*, 1988 WISC. L. REV. 353 (1988); Faludi, *The Reckoning: Safeway LBO Yields Vast Profits but Exacts A Heavy Human Toll*, Wall St. J., May 16, 1990, at 1, col. 6; *see also* CORPORATE TAKEOVERS: CAUSES AND CONSEQUENCES (A. Auerbach ed. 1988).

215 The fallout may be dated from the early 1990 Chapter 11 filings by Drexel Burnham Lambert, *see In re* Drexel Burnham Lambert Group, Inc., 112 Bankr. 584 (Bankr. S.D.N.Y. 1990), whose investment banking subsidiary had pioneered the use of low-grade, high-interest (so-called junk) bonds to finance numerous corporate takeovers; and Federated Department Stores and Allied Stores Corp., both of which had earlier been acquired in highly leveraged transactions by Toronto-based Campeau Corp. *See* Reibstein & Friday, *Seven Deadly Sins of Debt: Lessons from Campeau and Other Bankruptcies*, NEWSWEEK, Jan. 29, 1990, at 53.

216 The Texaco filing is discussed *supra* notes 61-63 and accompanying text.

Tactical filing cases, it will be recalled, are most readily distinguished by the usually more limited nature and size of the problem which has prompted the bankruptcy filing, and by an emphasis on deriving a litigation advantage from the procedural as opposed to substantive effects of the bankruptcy process.[217] Because of large companies' capacity to diffuse the harmful impact of discrete problems and disputes, most of the cases falling into this grouping involve somewhat smaller firms than those bearing the "Fortune 500" appellation. Unquestionably, Texaco is the exception in this regard, illustrating once again that the distinction between broad categories of cases blurs at the edges.[218]

Faced with the largest civil judgment ever entered against a private party,[219] and the prospect of that judgment becoming a lien on its assets,[220] it is initially tempting to portray Texaco as a party on the verge of a financial apocalypse.[221] Given that portrayal, the argument made by Texaco's management that resort to Chapter 11 was the only viable means of appealing the Pennzoil judgment[222] seems compelling. If accepted, Texaco would fall within the generally recognized rule that where the size of a judgment threatens a debtor's ability to stay in business, filing bankruptcy and obtaining the benefit of the automatic stay in

---

217 *See supra* text accompanying note 60.

218 For discussion on the role that grouping or cataloguing cases plays in our analysis, *see supra* text accompanying notes 176-77.

219 *See* Transworld Airlines, Inc. v. Texaco Inc. (*In re* Texaco Inc.), 92 Bankr. 38, 41 (S.D.N.Y. 1988).

220 Six days prior to the filing the U.S. Supreme Court had reversed lower federal court holdings that had enjoined Pennzoil from enforcing its judgment and declared that the Texas appeal bond requirement was unconstitutional. Pennzoil Co. v. Texaco Inc., 481 U.S. 1 (1987). Upon announcement of the Court's decision, the Texas Court of Appeals temporarily stayed enforcement of the judgment until April 13, 1987. Wall St. J., April 8, 1987, at 3, col. 1. Unless its Chapter 11 petition was filed by that time, absent a compromise between the parties, Texaco faced the prospect that Pennzoil would have been able to secure its judgment by bond or liens and thereby obtain a priority position in any subsequent bankruptcy. *See Texaco Finance Units File Bankruptcy*, OIL & GAS J., Apr. 20, 1987, at 19; *Bankruptcy Option: Texaco Files Petition For Chapter 11 as Talks With Pennzoil Collapse*, Wall St. J., Apr. 13, 1987, at 1, col. 6; *see also Texaco*, 92 Bankr. at 41 n.1 (noting that Pennzoil refused to extend a prior temporary agreement not to enforce its judgment against Texaco).

Theoretically, Texaco might have had as long as an additional 90 days to file if, in fact, the company lacked the net worth to pay the judgment. In that event, the transfer of any interest in its property to Pennzoil would have been voidable as a preference under 11 U.S.C. § 547(b) (1988). However, since a necessary element of all preferences is that the debtor be insolvent at the time of transfer—an open question in Texaco's case, *see supra* note 62—Texaco may have been loathe to take the risk. 11 U.S.C. § 547(b)(3) (1988).

221 In its decision upholding the district court's injunction prohibiting enforcement of the Pennzoil judgment pending appeal in the state courts, the Second Circuit noted that Texaco could not possibly meet the mandatory bond requirement to stay execution and that a $12 billion lien against its assets would seriously impair its ability to carry on its business. Texaco Inc. v. Pennzoil Co., 784 F.2d 1133, 1138 (2d. Cir. 1986), *rev'd*, 481 U.S. 1 (1987).

222 *Texaco*, 92 Bankr. at 41, 42; *see also* Wall St. J., Apr. 13, 1987, at 1, col. 6 (quoting Texaco President and CEO, James W. Kinnear, that the filing was " 'out of necessity' ").

lieu of posting a supersedeas bond does not constitute an act of bad faith.[223] Thus, while the clear two-party nature of the dispute motivating the filing would ordinarily generate a somewhat low score on the impact scale under these assumptions,[224] the Texaco case would still seem appropriate for Chapter 11 because of the orthodoxy of intention.

The conclusion that Texaco did not file in bad faith assumes, however, that the face value and real value of the Pennzoil judgment were roughly equal, and that the bankruptcy filing was necessary to buy the time required to reach a settlement financially palatable to Texaco. Both assumptions have been called into question in an article by Professors Mnookin and Wilson.[225] They submit that the $3 billion sum on which Texaco and Pennzoil eventually settled[226] could have been agreed upon without the necessity of the bankruptcy filing and, therefore, without the consumption of the additional resources which were committed to the various state and federal court appeals and, ultimately, to the Texaco reorganization itself.[227] Mnookin and Wilson's explanation for this behavior, which they observe resulted in a combined loss in value of $3.4 billion for the shareholders of both companies,[228] is that the risk of personal liability for breach of their fiduciary duty of care created an incentive for Texaco's management[229] to delay the settlement.[230] In support

223 *See supra* note 63 and accompanying text. In their concurring opinions, both Justices Brennan and Stevens suggested that Texaco's bankruptcy alternative supported the majority's conclusion that the federal district court should have abstained from issuing the injunction barring enforcement of the Pennzoil judgment on due process grounds. *See Texaco*, 481 U.S. 1, 18 (Brennan, J., concurring); *id.* at 32 n.6 (Stevens, J., concurring). *But see id.* at 28 n.* (Blackmun, J., concurring) (questioning the reality of the bankruptcy option for Texaco).

224 There can be no question that Texaco was not otherwise in need of financial rehabilitation, and that the central thrust of its reorganization plan was to reach a settlement with Pennzoil which, according to Texaco, could not be reached without the added leverage provided by the bankruptcy filing. *Texaco*, 92 Bankr. at 42 (with the exception of Pennzoil's, the Texaco reorganization plan provided for payment in full of all claims); Kirk v. Texaco Inc., 82 Bankr. 678, 679-80 (S.D.N.Y. 1988).

225 Mnookin & Wilson, *Understanding* Pennzoil v. Texaco, *supra* note 61.

226 *See In re* Texaco Inc., 84 Bankr. 893, 896 (Bankr. S.D.N.Y.) (describing the Pennzoil settlement and the other provisions of Texaco's reorganization plan), *aff'd*, 92 Bankr. 38 (S.D.N.Y. 1988).

227 Mnookin & Wilson, *supra* note 61, at 298. The authors present the hypothesis as a puzzle: why did settlement take so long? They see it as problematic because of their belief that rational bargaining behavior should secure a prompt compromise when it is clear that litigation costs exceed settlement costs and the parties have congruent expectations about the probable outcome of continued litigation. *Id.* at 315-16.

228 *Id.* at 297. This assertion is based on a study that charted the stock prices of Pennzoil and Texaco at high points during the controversy between the two companies. *See* Cutler & Summers, *The Costs of Conflict Resolution and Financial Distress: Evidence From the Texaco-Pennzoil Litigation*, 19 RAND J. ECON. 157 (1988). Because, according to Cutler and Summers, *id.* at 158, much of the combined loss in value was restored after the settlement, Mnookin and Wilson suggest that, absent exogenous influences, rational bargaining by the two managements would have produced a prompt settlement so that the billions in lost value could have been recouped as soon as possible. Mnookin & Wilson, *supra* note 61, at 315.

229 The authors use the term "management" to refer to the directors and executive officers of

of this assertion, made to explain why Texaco may have pursued a bargaining strategy that was at variance with obvious wealth-maximizing rationality,[231] Mnookin and Wilson point out that an integral component of Texaco's confirmed plan of reorganization was dismissal of pending shareholder derivative suits against managerial Texaco employees and indemnification for losses resulting should similar claims be asserted in the future.[232]

While Mnookin and Wilson's suggestion that the Texaco filing was prompted by management's conflict of interest has been challenged,[233] for our purposes it makes no difference if they are right or wrong.[234] Instead, we find it valuable to contemplate what the impact of Mnookin and Wilson's thesis would have been had it been proven to the satisfaction of the bankruptcy court. While $3 billion is no paltry sum, even for

---

Texaco who, in fact, had been named as defendants in various shareholder derivative suits charging breach of fiduciary duty. *Id.* at 316-17. Professor Baird and Dean Jackson have observed that, in some instances, the managers of a corporation who make the decision to enter Chapter 11 do so for personal reasons rather than because of a belief that bankruptcy represents the best forum in which to adjudicate rights to the firm's assets. *See* Baird & Jackson, *supra* note 6, at 125-26.

230 Mnookin and Wilson point to the Delaware Supreme Court's infamous 1985 decision, Smith v. Van Gorkom, 488 A.2d 858 (Del. 1985), as making the prospect for personal liability a much starker reality for Texaco's management than had theretofore been the case under Delaware corporate law. Mnookin & Wilson, *supra* note 61, at 318-21. The court in *Van Gorkom* surprised many corporate lawyers and managers with its holding that directors who were grossly negligent in failing to inform themselves about a proposed transaction could not claim the protection of the business judgment rule when the wisdom of their decision was challenged by disgruntled shareholders.

231 In addition to this "agency problem" explanation for why Texaco extended settlement negotiations and eventually sought sanctuary in Chapter 11, Mnookin and Wilson also proposed that the bargaining posture of the two parties placed them in a kind of "prisoners' dilemma" scenario where their respective efforts to obtain bargaining leverage inevitably produced an outcome in which both parties suffered financially. *Id.* at 328-29.

232 *Id.* at 323. The relevant provisions of the plan are discussed in *Texaco*, 84 Bankr. at 896, 903-04. *See also* Kirk v. Texaco Inc., 82 Bankr. 678 (S.D.N.Y. 1988) (affirming the bankruptcy court's approval of the debtor's disclosure statement over the objection of certain shareholders of the debtor).

233 *See* Bundy, *Commentary on "Understanding* Pennzoil v. Texaco*": Rational Bargaining and Agency Problems*, 75 VA. L. REV. 335 (1989) (questioning Mnookin and Wilson's assumption that both parties similarly evaluated the expected outcome of the litigation, and that Texaco's directors were influenced to a significant degree by the risk of personal liability); *see also* Lax, *Commentary on "Understanding* Pennzoil v. Texaco*": Market Expectations of Bargaining Inefficiency and Potential Roles for External Parties in Disputes Between Publicly Traded Companies*, 75 VA. L. REV. 367 (1989) (suggesting that delay in settlement might have been attributable to divergent interests among Texaco directors as well as between the Texaco directors as a group and the company).

234 As an aside, while *Smith v. Van Gorkom* did widely capture the concerned attention of corporate managers of public companies, its holding presented a much clearer cause for alarm in cases of directorial nonfeasance rather than misfeasance. That is, while *Van Gorkom* might be read to suggest that the business judgment rule may not be invoked to shield uninformed directorial decisions made without the exercise of reasonable judgment, it would be a stretch to interpret the decision as depriving directors who make informed but costly decisions of all protection under the business judgment rule. *See generally* R. CLARK, CORPORATE LAW 128-29 (1986).

a company the size of Texaco,[235] the discounting of the face amount of the Pennzoil judgment by seventy-five percent makes the question of imminent financial ruin, and thereby orthodox intent, far more problematic. If to this is added convincing evidence that Texaco's senior management engaged in a course of self-interested conduct designed to circumvent the kind of conflict of interest and fiduciary duty claims which long have been the province of the state courts[236] and legislatures,[237] the case for dismissal on grounds of bad faith becomes indeed convincing. As we indicated, in our view the Texaco filing has always scored somewhat lower than other public company filings on the impact scale because, notwithstanding its notoriety, the effects of the filing were largely contained.[238] Although it might be interesting to speculate who would be the proper party to raise this challenge,[239] we think that if the facts as

---

[235] For the year ended December 31, 1985 (the year in which the original Pennzoil verdict was entered), Texaco had gross revenue in excess of $47 billion and net income in excess of $1.2 billion. N.Y. Times, Apr. 13, 1987, at D4, col. 2.

[236] Corporate directors' duty of care has its roots in ancient common-law agency principles. *See generally* RESTATEMENT (SECOND) OF AGENCY § 379 (1958); 3A S. FLANAGAN & C. KEATING, FLETCHER CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS § 1029 (rev. perm. ed. 1986); *see also* W. SELL, AGENCY § 24 (1975) (discussing the unique nature of the relationship between directors and the corporation). Therefore, the law governing the conduct of corporate fiduciaries has been left to regulation by state, not federal, corporation law. *See* Santa Fe Indus. v. Green, 430 U.S. 462, 478-79 (1977).

[237] Most states have seen fit to codify the standard of care owed by corporate officers and directors. *See, e.g.*, MODEL BUSINESS CORP. ACT § 8.30(a) (1969) (rev. 1984); CAL. CORP. CODE § 309 (West 1990); N.Y. BUS. CORP. LAW § 717 (McKinney Supp. 1990); *see also* AMERICAN LAW INSTITUTE, *Principles of Corporate Governance: Analysis and Recommendations*, § 4.01 (Discussion Draft no. 4, 1985). In response to *Van Gorkom*, and its effect on the cost and availability of directors and officers' liability insurance, a large majority of the states—including, effective July 1, 1986, Delaware—have amended their corporations codes in the past five years to shield managers from personal liability for breaches of their duty of care. *See generally* DEL. GEN. CORP. LAW § 702(b)(7) (Supp. 1990); The Committee on Corp. Laws, *Changes in the Revised Model Business Corporation Act—Amendment Pertaining to the Liability of Directors*, 45 BUS. LAW. 695 (1990); Hanks, *Evaluating Recent State Legislation on Director and Officer Liability Limitation and Indemnification*, 43 BUS. LAW. 1207 (1988).

[238] In an effort to minimize the impact of its filing on ordinary business operations, only Texaco Inc. and two finance units were placed in Chapter 11, leaving all of Texaco's operating subsidiaries free from direct bankruptcy court supervision. *See* Wall St. J., Apr. 13, 1987, at 1, col. 6; *cf.* Gross & DeNatale, *It Won't Be Business as Usual: Texaco Files for a Traumatic Future*, N.Y. Times, Apr. 19, 1987, at C3, col. 1 (noting that Texaco's filing resulted in court-imposed constraints on the entire organization's operations). Ultimately, Texaco was able to confirm a reorganization plan providing for full cash payment plus post petition interest for all unsecured creditors other than Pennzoil. *See In re* Texaco Inc., 84 Bankr. 893, 895 (Bankr. S.D.N.Y.), *aff'd*, Transworld Airlines, Inc. v. Texaco Inc., 92 Bankr. 38 (S.D.N.Y. 1988). To be sure, Texaco's plan was exceptional in this respect. Successful and expeditious reorganizations are not the norm under Chapter 11. *See* LoPucki, *The Debtors in Full Control—Systems Failure Under Chapter 11 of The Bankruptcy Code?*, 57 AM. BANKR. L.J. 99, 100-01 (1983) (part 1).

[239] Most good faith challenges are raised by creditors. However, if Mnookin and Wilson's thesis is correct, the party with the greatest interest in jettisoning the proceeding should have been Texaco itself. After all, according to Mnookin and Wilson, the company had been unnecessarily driven into a costly bankruptcy proceeding by its directors who were placing their own interests ahead of those

hypothesized were so placed before a court, the judge could only retain jurisdiction over the proceeding by a decision, conscious or subliminal, to expand the scope of the bankruptcy process beyond its current parameters.[240]

Another area where we believe our proposed analysis would prove useful is in connection with environmental cleanup obligations,[241] currently a subject of much attention and controversy. While the Bankruptcy Code makes no special provision for environmental claims, in *Midlantic National Bank v. New Jersey Department of Environmental Protection*[242] the Supreme Court did acknowledge that environmental cleanup obligations might, to some extent, be treated differently from other general unsecured claims. Specifically, the court held that a bankruptcy trustee may not abandon property[243] containing hazardous waste without first making provision for protecting the public health and

---

of the corporation. However, since Texaco, acting through its managers, had already made the voluntary decision to seek bankruptcy protection, the likelihood of the party most directly affected raising the challenge would be remote indeed. Thus, the real dispute was between the owners and managers of the company and it would be left to equity security holders to assert the charge of bad faith derivatively. Technically, authority for shareholders' standing to do so can be found in the Code itself. *See* 11 U.S.C. § 1109(b) (1988). However, rights which belong to the debtor corporation, even though assertable and usually asserted by others outside of bankruptcy, are generally regarded as property of the estate which may be asserted only by the trustee. *See generally* American Nat'l Bank of Austin v. MortgageAmerica Corp. (*In re* MortgageAmerica Corp.), 714 F.2d 1266 (5th Cir. 1983). On the other hand, in a Chapter 11 case where the debtor acts as debtor-in-possession and assumes the rights and duties of the trustee, courts have recognized the right of third parties to maintain actions on behalf of a recalcitrant, self-interested debtor. *See, e.g.*, Coral Petroleum, Inc. v. Banque Paribas-London, 797 F.2d 1351, 1363 (5th Cir. 1986); *see also In re* Xonics Photochemical, Inc. 841 F.2d 198, 203 (7th Cir. 1988) (recognizing that a creditor may assert the debtor's right derivatively when the creditor can convince the court that the debtor has shirked its responsibilities).

240 This is generally consistent with our view that there is a temporal component which must be factored into any discussion about bankruptcy policy and the scope of the process. *See supra* notes 155-56 and accompanying text. We do not, however, absolutely rule out the possibility of simply a wrong or bad decision. That is, fully intending to apply existing doctrine consistent with prevailing policy, a judge may nonetheless come to a conclusion at variance with the current state of evolution. By no means could retention of jurisdiction in such a situation fairly be characterized as representing a purposeful response to a perceived shift in societal attitudes about the proper role of bankruptcy law and proceedings. Yet, in a common-law system, once on the books, if not overturned, the case stands and offers itself as precedent in future decisions. Of course, if clearly out of step with the underlying norms and expectations of the community, the case will largely be ignored or even discredited in connection with the adjudication of similar disputes in the future. However, when only slightly beyond the pale of existing authority regarding acceptable uses of bankruptcy process (which might account for the aberrant result to begin with) that decision may very well form an essential link in the inexorable development of the law, regardless of the inadvertant manner by which it came to be.

241 *See supra* note 65 and accompanying text.

242 474 U.S. 494 (1986).

243 The Bankruptcy Code gives the trustee (or debtor-in-possession) power to abandon property that is burdensome or of inconsequential value to the estate, and requires only that the trustee give notice of the proposed abandonment. 11 U.S.C. § 554(a), (b) (1988).

safety.[244] Subsequent cases, however, have failed to agree on either the scope of this exception or the circumstances (in terms of the imminency of harm to the public's health and safety) under which it obtains.[245] Concomitantly, while most cases decided since *Midlantic* have reasoned that if property may not be abandoned without remedying the state environmental law violations, then neither may it be retained without doing so,[246] they have failed to agree on the extent of compliance required.[247]

What, then, should be the response to a debtor that files a Chapter 11 bankruptcy petition in reaction to an order from a state or federal environmental regulatory agency to clean up property contaminated with hazardous waste? The answer depends on where the case falls along the intent and impact axes we have described. As in most other contexts, an enterprise that is not only solvent but also relatively stable financially should not find a receptive host in the bankruptcy court.[248] Orthodoxy of intent remains an important threshold consideration. When the extent or uncertainty over the extent of cleanup costs threatens a company's

---

244 *Midlantic*, 474 U.S. at 506-07. The Court concluded that, notwithstanding any express limitations, "Congress did not intend for § 554(a) to pre-empt all state and local laws. The Bankruptcy Court does not have the power to authorize an abandonment without formulating conditions that will adequately protect the public's health and safety." *Id.*

245 *Compare In re* Peerless Plating Co., 70 Bankr. 943, 947 (Bankr. W.D. Mich. 1987) (in most instances, a trustee may not abandon property with less than full compliance with environmental cleanup obligations) *with In re* Oklahoma Ref. Co., 63 Bankr. 562, 565 (Bankr. W.D. Okla. 1986) (*Midlantic* requires only that the bankruptcy court take state environmental laws and obligations into consideration in deciding on the trustee's motion for abandonment). *See also In re* Microfab, Inc., 105 Bankr. 161, 169 (Bankr. D. Mass. 1989), wherein, siding more or less with *Peerless*, the court concluded that *Midlantic* requires full compliance with environmental laws that are reasonably calculated to protect the public health and safety from immiment harm and do not " 'interfere with the bankruptcy adjudication itself.' " However, the court acknowledged that a trustee cannot be ordered to perform an obligation the cost of which exceeds the resources of the estate. *Id.* (citing Borden, Inc. v. Wells-Fargo Bus. Credit (*In re* Smith-Douglass, Inc.), 856 F.2d 12, 17 (4th Cir. 1988)).

246 Cases recognizing that the cost of cleaning up contaminated property is properly chargeable as a priority expense of administration include: *In re* Smith-Douglass, Inc., 856 F.2d 12, 17 (4th Cir. 1988); *In re* Wall Tube & Metal Prods. Co., 831 F.2d 118, 123 (6th Cir. 1987); *In re* Better-Brite Plating, Inc., 105 Bankr. 912, 916 (Bankr. E.D. Wis. 1989).

247 *Compare In re* FCX, Inc., 96 Bankr. 49, 55 (Bankr. E.D.N.C. 1989) (only costs reasonably required to remove threat of immediate harm will be given administration expense first priority) *with In re* Microfab, Inc., 105 Bankr. 161, 169 (Bankr. D. Mass. 1989) (full compliance required where trustee has sufficient assets to do so). The question of when an environmental claim is deemed to arise also has been the subject of some disagreement. *Compare* United States v. Chateaugay Corp. (*In re* Chateaugay Corp.), 112 Bankr. 513, 525 (S.D.N.Y. 1990) (rejecting the government's position that a claim arising out of a pre-petition release or threatened release of hazardous waste does not arise until the environmental agency actually incurs costs to clean up the contaminated site) *with* Jensen v. Bank of Am. N.T. & S.A. (*In re* Jensen), 114 Bankr. 700, 703-04 (Bankr. E.D. Cal. 1990) (a premature environmental claim is unlike a tort that has been committed but not yet sued upon, and thus does not necessarily arise at the time the violation occurs). Importantly, however, the *Chateaugay* court did recognize that cleanup costs assessed post-petition, even if for a pre-filing release, are entitled to administrative expense priority. 112 Bankr. at 525-26.

248 *See supra* note 66 and accompanying text.

continued survival, however, the next step must be taken. Recalling that the impact quotient takes into account the breadth of interests directly affected by the filing, the immediacy of those effects, and the existence of non-bankruptcy institutions to respond to the particular crisis inducing the bankruptcy filing, we conclude that in most environmental cases impact would be considerable.

Thus, as with any case arising out of our third category, it becomes necessary to look beyond the fact that the filing was prompted by a dispute between two parties and to inquire into the effects, actual and potential, of that dispute and its possible resolution on both the debtor's financial condition and the condition of the community in which the debtor exists and interacts. It is precisely that inquiry which is forced by the calculus we have put forth. The calculus calls attention to the factors at work in explaining why decided cases were resolved as they were, and, in so doing, it provides a framework for thinking about how any future case, no matter how factually disparate from its predecessors, is likely to be decided. Moreover, when a new decision is rendered, whether or not its outcome comports with prior prediction, we are able to detect and observe the dynamic of the good faith doctrine at work.

This is not to assert that every case that departs from current thinking about the scope of bankruptcy policy rises to the dignity of a working example of the evolutionary process. We do not believe that every decision is right by definition. Rather, each decision that signals a departure invites close study. A case that runs counter to the result predicted by the calculus must offer a reasoned basis for its outcome. If it does not, it is a random departure and of no value insofar as the evolution of bankruptcy policy is concerned.

CONCLUSION

To say that the law evolves in sympathy with the social and economic institutions it serves is by no means to lay claim to a revelation. Still, the statement bears repeating as it embodies a vigorous concept of genuine utility in making sense of the positive law. In other words, to say the law is in constant flux is not merely to make an observation about the nature of law: it is to arm ourselves with a capacious aid to analysis of knotty juristic issues of theoretical and practical moment.

In this Article, by proceeding from the assumption that the scope of bankruptcy is determinate but evolving as a result of exogenous demands upon it, we have been able to formulate a calculus by which to describe the current state of bankruptcy policy and with which to speculate on possible future directions. In the course of this endeavor we found that questions concerning the role of the courts and the function of the good faith requirement in the evolutionary process presented themselves naturally and obviously for consideration. So perceived, the good faith doctrine was transformed from a stale platitude called upon in despair of a clear rule to "do equity," to a flexible instrument providing standards in an environment where the boundaries of bankruptcy policy are constantly tested. We have been moved, as a result, to ruminate (sub silentio) about the role of good faith and other familiar, time-tested favorites of the law in other contexts as well.[249]

Finally, we have been led to assert that the evolution of bankruptcy policy and purposes is observable and describable from the positive law. It is from this assertion that we were challenged to construct a simple calculus with a dynamic component to accommodate the dynamic system it seeks to describe. The extent to which we have succeeded in this endeavor we leave the reader to decide; but we are convinced the process was informative and worthwhile. If the notion of the law in flux is not new, it is an idea that should not be put aside until wrung dry of its every application in legal interpretation, analysis, and reform.

249 Analysis along the lines of that undertaken here might be profitably applied to longstanding common law or other equitable doctrines employed in various contexts by courts, such as the doctrines of estoppel, waiver, bona fide purchase, and those relating to the obligations of fiduciaries, actual and constructive.