CREDITORS' COMMITTEES UNDER CHAPTER 11 OF THE UNITED STATES BANKRUPTCY CODE: CREATION, COMPOSITION, POWERS AND DUTIES

PETER C. BLAIN*
DAVID A. ERNE**

I. INTRODUCTION

The United States Bankruptcy Code (Code),1 which became effective October 1, 1979,2 gives creditors' committees a much broader and more visible role in Chapter 11 reorganization proceedings than that which they assumed in arrangement proceedings under Chapter XI of the pre-Code law.3 This new power, taken together with the lesser standing given by the Code to the court to participate in the day-to-day administration of cases,4 provides committees with the opportunity to assert far greater influence over the outcome of reorganization proceedings than was previously possible. However, recent studies of the role of committees under the Code conclude that they often fail to exercise the broader powers now available to them and, in fact, in many cases fail to function effectively in any meaningful way.5

Failure of committees to always act fully in their own best interests might be attributed to many causes, including

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* B.S., University of Wisconsin-Stevens Point, 1971; J.D., Georgetown University Law Center, 1978; associate, Reinhart, Boerner, Van Deuren, Norris & Rieselbach, S.C., Milwaukee, Wisconsin.


4. See, for example, section 341(c) of the Code, which provides that the court may not preside at, or attend, the first meeting of creditors.

5. See infra note 160 and accompanying text.
lack of experience, lack of knowledge about the law and concern that even a significant effort will not substantially improve the creditors' position. There is often an unwillingness of committee counsel to commit substantial time if there is concern that funds may not be available to pay expenses of administration, including counsel fees.

This article will examine the functions of committees under the Code with the objective of providing a more complete understanding of their roles. The authors believe that greater insight into the creation and operation of Chapter 11 committees may help increase their effectiveness and the effectiveness of their counsel.

II. CREATION AND COMPOSITION OF COMMITTEES

A. Initial Appointment

Pursuant to section 1102(a)(1) of the Code, a committee of creditors holding unsecured claims is to be appointed by the court as soon as possible after the entry of an order for relief.\(^6\) In pilot districts,\(^7\) the United States Trustee made the initial appointment.\(^8\) Committees of creditors appointed under section 1102(a) ordinarily consist of "persons," willing to serve, that hold the seven largest "claims" against the debtor.\(^9\)

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6. Although this section is directive rather than permissive, unsecured creditors' committees are not appointed in every Chapter 11 proceeding. One study, for example, reflects that unsecured creditors' committees were appointed in only 40% of the Chapter 11 cases filed in the Western District of Missouri during the first year after the effective date of the Bankruptcy Code. See LoPucki, The Debtor in Full Control—Systems Failure Under Chapter 11 of the Bankruptcy Code? (First Installment), 57 Am. Bankr. L.J. 99, 100 (1983).


9. Id. § 1102(b)(1). Although committees are usually comprised of the largest claim or interest holders, this is not always the case. In In re White Motor Credit Corp., 27 Bankr. 554 (Bankr. N.D. Ohio 1982), the district court affirmed the bankruptcy court's appointment of four small shareholders and two large shareholders to the equity security holders' committee pursuant to section 1102(b)(2). These shareholders were the only equity holders responding to the request to serve on the committee.
The term "persons" has been defined to exclude governmental units. Thus, relying on the definition of "persons" in section 101(30), one court has denied the application of a school district to be represented on the creditors' committee. Other courts, in analyzing the definition of "claims" in section 101(4), have noted that the term includes disputed claims and have permitted holders of such claims to be appointed to the creditors' committee. Holders of both unsecured and secured claims are also permitted to serve on the committee if they otherwise meet the requirements for membership.

Courts have distinguished between individual holders of claims against the debtor, and associations, such as labor unions, which represent such claim holders. In In re Altair Airlines, Inc., for example, the bankruptcy court found that although the Airline Pilots Association International represented pilots who held claims against the debtor, the union itself was not a claim holder and, therefore, not a creditor as defined in section 101(9). Accordingly, the court denied the union's request to be appointed to the committee.

While the district court affirmed this position, the Third Circuit Court of Appeals reversed, noting that the union was an unincorporated association and was therefore an "entity" within the meaning of section 101(9) of the Code. The court also found that the union had a "claim" within the meaning of section 101(4), relying upon federal common law which permitted unions to sue to recover unpaid wages and vacation pay. In remanding to the district court for the entry of an order directing the bankruptcy court to grant the union's application for appointment to the creditors' com-

10. 11 U.S.C. § 101(30) (1982) provides that "‘person’ includes individual, partnership, and corporation, but does not include governmental unit.”
13. 5 COLLIER ON BANKRUPTCY § 1102.01[2] (15th ed. 1983) [hereinafter cited as COLLIER].
15. Id. at 225. See also In re National Equip. & Mold Corp., 33 Bankr. 574, 576 (Bankr. N.D. Ohio 1983).
17. Id. at 90.
18. Id.
mittee, the Third Circuit rejected as "too metaphysical" the
debtor's argument that the union could not "collect" wages,
but only cause them to be passed through to its members.19

The Third Circuit in *Altair* also criticized the reasoning
of *In re Schatz Federal Bearings Co.*,20 in which the United
States Bankruptcy Court for the Southern District of New
York concluded that a union could not enforce the claims of
its members under the Employee Retirement Income Secur-
ity Act of 1974, as amended (ERISA),21 and therefore would
ordinarily not be a creditor in its own right.22 However,
because the debtor's funding obligation under the pension plan
for employees was incorporated by reference into its collect-
tive bargaining agreement, the *Schatz* court found that the
union would have standing to sue for past due pension obli-
gations under the Taft-Hartley Act,23 and was therefore a
creditor under section 109(9) of the Code. On this narrow
basis, the *Schatz* court granted the union's application to be-
come a member of the committee.24

Courts generally have allowed creditors appointed as
members of committees to designate agents, such as attor-
neys, to serve as members on their behalf. However, where
an attorney represents more than one creditor, the attorney
may sit as a designee of only one of them.25 Although courts
permit lawyers to be designated as creditor representatives,
they strongly encourage creditors to appoint persons en-
gaged in business to serve on the creditors' committee. Such
persons, reason the courts, possess greater insight into the
business affairs of the debtor and are therefore better able to
assist the committee in fulfilling its functions.26

19. *Id.*
20. 5 Bankr. 543 (Bankr. S.D.N.Y. 1980).
24. *Schatz Federal Bearings*, 5 Bankr. at 548. *But see In re Liberal Mkt., Inc.*, 11
Bankr. 742, 746 (Bankr. S.D. Ohio 1981) (unions added to the creditors' committee
without comment).
26. See, e.g., *id.* at 267.
B. Changes in Committee Membership

Pursuant to section 1102(c), upon request of a party in interest, after notice and a hearing, the court has the power to change the membership or size of a committee if the committee is not representative of the different kinds of claims or interests to be represented. For the purpose of raising an objection to the committee composition, "parties in interest" include the debtor, other creditors and the United States Trustee in pilot districts. The term does not include the court, however, and the court has no power to modify committee composition sua sponte.

1. Conflicts of Interest

Successful challenges to committee composition have usually involved actual or potential conflicts of interest, or risks of compromise of information that is confidential as to the debtor because it involves committee deliberations, or is confidential as to competitors because it involves the affairs of the debtor. Insiders have generally, although not always, been barred from serving as members. In *In re Glendale Woods Apartments, Ltd.*, for example, the bankruptcy court removed two committee members found to be insiders, stressing the risks to confidentiality of communication among committee members.

27. See, e.g., *In re AKF Foods, Inc.*, 36 Bankr. 288 (Bankr. E.D.N.Y. 1984) (court had power to expand a committee although such enlargement was not necessary to ensure adequate representation of creditors).
31. COLLIER, supra note 13, at § 1102.01[3]. See also *In re Kontaratos*, 15 Bankr. 298 (Bankr. 1st Cir. 1981), in which the Bankruptcy Appellate Panel reversed a bankruptcy judge who ordered the United States Trustee to investigate allegations of fraud lodged against committee members. In its decision, the court stressed that proceedings to change committee membership under section 1102(c) were adversary matters requiring proof on one side and either acquiescence or defense on the other. *Id.* at 301.
32. 25 Bankr. 414 (Bankr. D. Md. 1982). See also *In re Daig Corp.*, 17 Bankr. 41 (Bankr. D. Minn. 1981), in which the court removed a creditor whose father was the chairman of the board of the debtor, and *In re Penn-Dixie Indus.*, Inc., 9 Bankr. 941 (Bankr. S.D.N.Y. 1981), where an appointee to the equity committee who also sat on the board of directors of the debtor was challenged and removed from the committee. In both cases the respective courts stressed the need to protect the confidentiality of committee proceedings.
In contrast, in *In re Vermont Real Estate Investment Trust,* the United States Bankruptcy Court for the District of Vermont refused to deny committee membership to the wife of the former executive officer of the debtor, who was an insider under section 101(25) of the Code. The insider creditor was also a co-defendant with her husband in a state lawsuit alleging fraudulent involvement in certain of the debtor's prior activities. The court analyzed section 1102(b)(1) and found that because insiders were not specifically excluded from service on the committee, the petitioning creditor was entitled to membership. Although the court required the creditor to refrain from participating in any discussion regarding the lawsuit involving her, it did not seem concerned about other confidential communications to which she might have been privy, even though the court noted that the objecting creditors were concerned about the risk to confidentiality in general. Because the success of a reorganization proceeding may depend on the aggressive and sometimes adversarial participation of a committee relying upon confidential information, precluding insiders from sitting on a committee under any circumstances is the better reasoned view.

Protecting information which is confidential as to competitors was at issue in *In re Wilson Foods Corp.,* where an Oklahoma bankruptcy court denied a direct competitor's request that it be permitted to serve on the creditors' committee. The debtor contended that the creditor's service on the committee would impair the debtor's ability to deal candidly with the committee. Additionally, the court noted that if the competitor did not take advantage of confidential information gained through committee membership, the competitor's shareholders might have cause to complain.

34. Unproven allegations of fraud have been held not to be sufficient cause to warrant removal from a committee. See infra note 43 and accompanying text.
35. *Vermont Real Estate Inv. Trust,* 20 Bankr. at 35.
36. *Id.* at 36.
37. *Id.* at 33.
"Conflicting interests and divided loyalties," said the court, "have no place on a committee of creditors."\(^{39}\)

The *Wilson* court's position is not universally held, however. In *In re Penn-Dixie Industries, Inc.*\(^{40}\) the United States Bankruptcy Court for the Southern District of New York permitted a creditor to retain its committee seat, although the creditor had filed documents\(^{41}\) with the Securities Exchange Commission disclosing its intention to acquire ownership of the debtor. The court found that the likelihood of the creditor's misuse of confidential information would be purely speculative. In any case, the Rules of Bankruptcy Procedure, concluded the court, contained provisions which could be invoked to protect against disclosures of confidential information or breaches of fiduciary duties.\(^{42}\)

2. Other Grounds for Removal

Absent either an overt threat to confidential information or other blatant conflict of interest, courts generally will not modify the membership of a creditors' committee. Unproven allegations of fraud, for example, have been held not to be sufficient cause to deny committee membership to a creditor.\(^{43}\) Nor has lack of sympathy for the debtor's reorganization efforts persuaded a court to remove a committee member. In *In re M.H. Corp.*\(^{44}\) an attorney representing a number of creditors appeared at the first meeting of creditors at which the committee was to be formed and stated that his clients would object to any plan the debtor proposed and would prefer to see the debtor liquidated under Chapter 7. The debtor's counsel objected vigorously to the creditors', or the attorney's, membership on the committee. The Ohio

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39. *Id.* at 272.
41. Schedule 13-D was filed pursuant to SEC Rule 13(d), 17 C.F.R. § 240.13d-1 (1983).
42. *Penn-Dixie*, 9 Bankr. at 940.
43. *See, e.g.*, *In re* Vermont Real Estate Inv. Trust, 20 Bankr. 33 (Bankr. D. Vt. 1982); *In re* Bennett, 17 Bankr. 819 (Bankr. D.N.M. 1982). In *In re Kontaratos*, 10 Bankr. 373 (Bankr. D. Maine 1981), the judge was sufficiently concerned about allegations of fraud (the charging of interest at 350% per annum) that he directed the United States Trustee to investigate the charges. The First Circuit Bankruptcy Appellate Panel reversed, stressing that such allegations had to be proven by resort to the adversarial system. *In re Kontaratos*, 15 Bankr. 298, 301 (Bankr. 1st Cir. 1981).
44. 30 Bankr. 266 (Bankr. S.D. Ohio 1983).
45. The first meeting of creditors is held pursuant to 11 U.S.C. § 341 (1982).
bankruptcy court, noting that the Code did not preclude committee membership to unsympathetic parties, confirmed the appointment.\textsuperscript{46}

Similarly, holding the preponderance of unsecured claims in a case does not cause a creditor to be "[un]representative of the different kinds of claims or interests to be represented,"\textsuperscript{47} as section 1102(c) requires before removal is warranted. In \textit{In re American Federation of Television \& Radio Artists},\textsuperscript{48} the bankruptcy court refused to remove from the committee a creditor who held ninety-eight percent of the unsecured claims against the debtor. In so holding, the court specifically noted that there was neither a conflict of interest with any other creditor nor a close alliance with the debtor which would support such removal.\textsuperscript{49}

\textbf{C. Committees in Addition to the Official Creditors' Committee}

Section 1102(a)(2) provides that, in addition to the official creditors' committee, the court may appoint other creditors' committees or an equity security holders' committee upon request of a party in interest, if the court determines that such committees are necessary to ensure adequate representation of the creditors or interest holders in the case.\textsuperscript{50} The Securities and Exchange Commission, which pursuant to section 1109(a) is given the specific right to be heard on any issue in a case, frequently requests the appointment of an equity security holders' committee in cases involving large numbers of equity holders.\textsuperscript{51}

Although an equity security holders' committee is the only type of additional committee specifically mentioned in section 1102(a)(2), the term "other committees" has been given broad interpretation. Examples of "other committees"

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\textsuperscript{46} \textit{M.H. Corp.}, 30 Bankr. at 267.
\textsuperscript{47} \textit{11 U.S.C. § 1102(c) (1982).}
\textsuperscript{48} \textit{30 Bankr. 772 (Bankr. S.D.N.Y. 1983).}
\textsuperscript{49} \textit{Id. at 776. See also In re Daig Corp., 17 Bankr. 41 (Bankr. D. Minn. 1981).}
\textsuperscript{50} As with appointment of the creditors' committee, in pilot districts the United States Trustee made appointments to the additional committees after order of the court. \textit{See 11 U.S.C. § 151102(b) (1982). See supra note 7 and accompanying text.}
\textsuperscript{51} \textit{See, e.g., In re White Motor Credit Corp., 27 Bankr. 554 (Bankr. N.D. Ohio 1982).}
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include committees of secured creditors,\textsuperscript{52} priority creditors,\textsuperscript{53} subordinated note holders,\textsuperscript{54} undivided interest holders,\textsuperscript{55} property owners,\textsuperscript{56} finance fund certificate holders,\textsuperscript{57} labor representatives,\textsuperscript{58} tort claimants\textsuperscript{59} and asbestosis litigants.\textsuperscript{60}

One of the major factors affecting a court's decision on the appointment of multiple committees in a case is the increased expense to the estate. Since the costs and expenses of a committee,\textsuperscript{61} as well as those of its counsel and of other professional persons employed by it under section 1103 of the Code, are administrative expenses under section 503. They are therefore entitled to priority under section 507 of the Code and will be paid before the claims of unsecured creditors. While in very large cases the direct impact on unsecured creditors may be relatively minor, in small to me-


\textsuperscript{57} See, e.g., \textit{In re} Western Farmers Ass'n, No. 79-02143 (Bankr. W.D. Wash. Dec. 10, 1979).

\textsuperscript{58} See, for example, \textit{In re} Wickes Companies, Inc., No. LA-82-06657-WL (Bankr. C.D. Cal. Apr. 24, 1982), where the court appointed an unofficial Labor Committee comprised of unions and benefit plans. The court directed the debtor to confer with the Labor Committee regarding developments in the case, but specifically provided that members of the Labor Committee would not be entitled to reimbursement under section 503 of the Code. Concerning the right of a committee to reimbursement of expenses or compensation generally, see \textit{infra} text accompanying notes 125-40.


\textsuperscript{60} See, e.g., \textit{In re} Johns-Manville Corp., No. 82-B-11656 (Bankr. S.D.N.Y. Aug. 26, 1982); \textit{In re} UNR Indus., Inc., No. 82-B-9841 (Bankr. N.D. Ill. July 29, 1982).

\textsuperscript{61} There is a split of authority on whether committee members are entitled to reimbursement of expenses incurred in connection with a case. See \textit{infra} text accompanying notes 125-40.
diem-sized cases the appointment of multiple committees could have a significant effect on the ultimate distribution to unsecured creditors.

A recent decision makes clear that when additional committees are appointed, their fees and expenses are entitled to equal priority with the fees and expenses of the unsecured creditors' committee. In *In re Wilnor Drilling, Inc.* the United States District Court for the Southern District of Illinois reversed the bankruptcy court's ruling that the fees and expenses of the investors' committee were subordinate to those of the official creditors' committee. Although the court acknowledged that the appointment of an unsecured creditors' committee was mandatory while the appointment of other committees was discretionary, it held that that factor alone was insufficient to warrant subordination of the investors' committee's expenses. The court concluded that the Code does not distinguish between the fees and expenses of various committees, and while the court had the power to equitably subordinate claims because of fraud, bad faith or inequitable conduct, those factors were not present.

D. Overlapping Committees

Some courts have strongly suggested that in cases which are being jointly administered but which have not been substantively consolidated, separate committees should be appointed for each debtor. In *In re White Motor Credit Corp.*, for example, an Ohio bankruptcy court denied the application of the debtors in possession in six related cases for the appointment of a single committee. Without separate committees, said the court, "[t]he presence of disinterested yet voting members could easily divert attention from legitimate committee activities (§ 1103) and chill the initiative which, hopefully, has been brought to the reorganization environment." This position is not universally held, however, and

62. 29 Bankr. 727 (Bankr. S.D. Ill. 1982).
63. *Id.* at 730-31.
64. 18 Bankr. 720 (Bankr. N.D. Ohio 1980).
other courts have appointed single committees for related debtors in jointly administered cases.  

III. POWERS AND DUTIES OF COMMITTEES

A. Appointment and Compensation of Counsel and Other Professionals

The powers and duties of a committee appointed under section 1102 are enumerated in section 1103. Recognizing the committee's need for professional assistance, Congress provided, in section 1103(a), that at a meeting of the committee, a majority of its members may authorize retention of attorneys, accountants and other agents. The ultimate employment of the professional selected is subject to prior court approval.

Section 1103(b) provides that a person employed by a committee may not represent any other entity connected with the case. This section has been construed to prohibit representation of more than one committee in related proceedings, as well as the representation of an individual committee member in addition to the committee as a whole. The obvious danger which the section seeks to avert is the committee and the second entity taking polar positions upon an issue, thus creating an irreconcilable conflict of interest. If the proscription of section 1103(b) is vio-


68. Id.

69. Id.


72. United States Bankruptcy Judge Ryan described the concern as follows: To avoid the manifestation of this conflict would serve both the best interests of the parties as well as the integrity of this court. Neither the appointment of special counsel once the conflicts materialize, nor the resignation of [the firm] (as they so willingly provide in their affidavits supporting the respective applications) would be as suitable as denying the creditors' applications in the first instance.

lated, one potential penalty is a denial of all compensation as provided in section 328(c) of the Code.

Compensation may be denied in other instances. For example, counsel may not be paid for administrative work which could have been done by the committee secretary, such as drafting notices to creditors, notifying creditors of meetings and drafting reports of creditors’ committees.\(^7\)

Compensation may also be denied to a committee’s counsel if court approval for employment is not obtained before the services are performed. Although some courts have granted such authorization \textit{nunc pro tunc} and thereupon allowed compensation,\(^7\) such orders are generally disfavored and other courts have denied compensation for unauthorized services, even where the services were rendered to the committee in good faith.\(^7\)

Additionally, all compensation requested is subject to court approval and must be reasonable in light of the circumstances relating to the particular case. Compensation requests are evaluated pursuant to the criteria set forth in section 330 of the Code. These criteria include “the time, the nature, the extent, and the value of such services.”\(^7\)

To a certain extent, compensation awarded to professionals may also depend upon the nature of the estate, even if the services provided otherwise meet the requirements of section 330. In \textit{In re S&S Industries, Inc.},\(^7\) a Michigan bankruptcy court refused to require a secured creditor to pay the fees of counsel to the creditors’ committee when there were no unencumbered assets in the estate. Rejecting the Committee’s request that the court apply section 506(c) of the Code, which permits a trustee to receive from a secured creditor reimbursement of expenses incurred in preserving the collateral, the court held “[s]ection 506(c) enables a trustee to recover from a secured creditor the reasonable necessary costs


\(^{74}\) \textit{See, e.g., In re Bill & Paul’s Sporthaus, Inc.,} 31 Bankr. 345 (Bankr. W.D. Mich. 1983) (order approving employment of committee counsel entered \textit{nunc pro tunc}).

\(^{75}\) \textit{See, e.g., In re Bear Lake West, Inc.,} 32 Bankr. 272 (Bankr. D. Idaho 1983) (court refused to authorize employment of committee counsel \textit{nunc pro tunc}).


and expenses 'of preserving, or disposing of,' encumbered property 'to the extent of any benefit to' such creditor. It does not confer this right upon a creditors' committee."

Although a secured party is free to consent to pay such fees, continued the court, such consent is not to be inferred from mere cooperation with the debtor.

Where, however, there are funds in the estate in excess of secured claims, committee counsel may be paid even if the unsecured creditors receive no distribution pursuant to a plan of reorganization. In In re Joyanna Holitogs, Inc., for example, a New York bankruptcy court awarded interim compensation to counsel for the unsecured creditors' committee, although no distribution to unsecured claimants was probable. The court noted that committee counsel is indispensable in every Chapter 11 proceeding where there are unsecured creditors, regardless of how much such creditors receive pursuant to a plan. It is only after proper investigation spearheaded by diligent counsel that a committee can evaluate a plan that provides little or nothing for unsecured creditors. To deny compensation to committee counsel because the creditors will not fare well, concluded the court, will discourage the investigation which is crucial in determining whether a plan is feasible.

B. General Powers of a Committee

In addition to specifically permitting a committee to retain professional advisors, the Code authorizes a committee of creditors or interest holders to fulfill the duties enumerated in section 1103(c):


79. S&S Indus., 30 Bankr. at 398. But see Wilson Freight Co. v. Citibank, N.A. (In re Wilson Freight Co.), 21 Bankr. 398 (Banrk. S.D.N.Y. 1982) (court awarded interim compensation to committee counsel in an "undersecured" Chapter 11 proceeding in which assets were less than the secured debt where the secured creditor ignored the bankruptcy judge's suggestion that the case be converted to a liquidation under Chapter 7).


81. Id. at 408.
(c) A committee appointed under section 1102 of this title may—

(1) consult with the trustee or debtor in possession concerning the administration of the case;

(2) investigate the acts, conduct, assets, liabilities, and financial condition of the debtor, the operation of the debtor's business and the desirability of the continuance of such business, and any other matter relevant to the case or to the formulation of a plan;

(3) participate in the formulation of a plan, advise those represented by such committee of such committee's recommendations as to any plan formulated, and collect and file with the court acceptances of a plan;

(4) request the appointment of a trustee or examiner under section 1104 of this title, if a trustee or examiner, as the case may be, has not previously been appointed under this chapter in the case; and

(5) perform such other services as are in the interest of those represented.\(^{82}\)

As the section suggests, a committee's role is basically advisory and not one of control of the debtor.\(^{83}\) In *In re UNR Industries, Inc.*,\(^ {84}\) for example, the United States Bankruptcy Court for the Northern District of Illinois declined to order the debtor to give the committee prior notice before implementing certain management decisions. Noting that the debtor in possession in a Chapter 11 proceeding is empowered to continue its operations without day-to-day input from creditors, the court concluded that if the committee believes that the debtor is not capable of proper management, the appropriate remedy is to move for the appointment of a trustee pursuant to sections 1103(c)(4) and 1104 of the Code.\(^ {85}\)

Committees are empowered under section 1103(c)(2) to investigate, among other things, the operations and financial affairs of the debtor. As noted previously, such investigation is crucial to the committee's ability to make an informed de-

\(^{82}\) 11 U.S.C. § 1103(c) (1982).

\(^{83}\) *COLLIER*, *supra* note 13, at § 1103.07[3].


\(^{85}\) Id. at 967. *See also In re Vancor Steamship Corp.*, 8 Bankr. 470 (Bankr. S.D.N.Y. 1981).
cision about the feasibility of a reorganization plan.\textsuperscript{86} In a
decision which may greatly enhance a committee’s power to
conduct such an investigation, the Eleventh Circuit Court of
Appeals held in \textit{International Horizons, Inc. v. Committee of
Unsecured Creditors (In re International Horizons, Inc.)},\textsuperscript{87}
that there exists no federal accountant-client privilege which
can be raised by a debtor to bar a committee’s access to
necessary financial information. The court cited to section
1103(c)(2)\textsuperscript{88} and concluded that the federal policy expressed
in 1103(c)(2) precluded the application of any such privilege
recognized under state law on the basis of comity.\textsuperscript{89}

Pursuant to section 1103(c)(3), a committee is also au-
thorized to participate in the formulation of a plan of reor-
ganization. This includes proposing a plan jointly with the
debtor,\textsuperscript{90} or proposing a separate plan altogether, assuming
that the debtor’s exclusive period to file a plan has expired or
has been terminated.\textsuperscript{91} A committee is further empowered
to advise its constituency about the merits of any plan pro-
posed.\textsuperscript{92} This very important function gives a committee
considerable leverage in negotiating the terms of a plan with
any proponent, and especially with the debtor. A negative
recommendation by a committee will frequently preclude a
plan’s acceptance\textsuperscript{93} or confirmation.\textsuperscript{94}

\textbf{C. Standing of a Committee}

1. Standing to Commence Legal Actions

Section 1103(c)(5) authorizes committees to “perform
such other services as are in the interest of those repre-
This broad grant of authority has been interpreted to permit a committee to participate freely in virtually every aspect of a case. However, one question has spawned a significant amount of litigation: whether a committee may institute legal action in its own name and intervene in actions commenced by others.

The right to commence actions is very important since debtors in possession may be reluctant or even unwilling to seek recovery of assets, such as avoidable preferences or fraudulent conveyances, from trade creditors whose goodwill may be vital to their postreorganization prospects. Such reluctance may prejudice the creditor body as a whole. Because a committee is a temporary body charged with ensuring equal treatment for all creditors, it may be the ideal party to prosecute such actions. In so doing, the committee may improve the prospects of creditors generally, either by increasing the total distribution creditors receive or, at a minimum, by facilitating a successful reorganization which will cure the financial ills of a valued customer or supplier.

A majority of courts have recognized a committee's standing to sue, although they have disagreed over whether that right arises under section 1103(c)(5) or instead under section 1109(b) of the Code. Cases finding that creditors' committees have an implied right to commence adversary proceedings under section 1103(c)(5) have generally involved situations in which the debtor in possession, or the trustee, unjustifiably refuses to act and the committee ob-

97. As Bankruptcy Judge Babitt of the Southern District of New York has put it: [I]t must surely be well known that Chapter 11 debtors seeking to reorganize and thereby reenter the commercial world are understandably loath to sue those whose support they need post-reorganization. The court here refers to suppliers, servicepeople, lenders and the like and not to a debtor's insiders who have been treated too generously by a debtor on the eve of its bankruptcy petition.

tains the prior consent of the court to bring an action.98 In
Committee of Unsecured Creditors v. Monsour Medical
Center (In re Monsour Medical Center),99 for example, a
Pennsylvania bankruptcy court found that while there is no
express authority in the Code which permits a creditors'
committee to institute an action, a committee has an implied
right to sue to avoid preferences and fraudulent conveyances
when the debtor in possession refuses to act, but such refusal
is not sufficient to support the appointment of a trustee. Any
suit instituted, concluded the court, must be commenced on
behalf of the debtor.100

The implied right of a committee to sue has been ex-
tended to causes of action other than those which seek to
recover previously transferred assets. Committees have been
found to have standing, for example, to bring federal anti-
trust actions,101 seek declaratory relief regarding the exist-
ence of leases,102 assert rights in unsold timeshare
units,103 participate in reclamation actions,104 seek subordination of

98. Receiving the prior authorization of the court may not always be required.
See, e.g., Gander Mountain, Inc. v. Impact Indus., Inc. (In re Gander Mountain,
Inc.), 29 Bankr. 260 (Bankr. E.D. Wis. 1983). But see Chemical Separations Corp. v.
Foster Wheeler Corp. (In re Chemical Separations Corp.), 32 Bankr. 816 (Bankr.
E.D. Tenn. 1983); Unsecured Noteholders' Comm. v. First Nat'l Bank & Trust Co. (In
Ohio 1983), which suggest the contrary. The better approach is to obtain court ap-
proval in advance of commencing actions, where possible. Where a trustee or debtor
in possession is diligently pursuing legal action, committees have been barred from
proceeding in their own name. See, e.g., Official Creditors' Comm. v. Alloy Automo-
BANKR. CT. DEC. (CRR) 1112 (Bankr. E.D. Pa. 1983) (individual creditor held not to
have a right to seek subordination of a claim under section 510(c) where trustee had
already filed a complaint to subordinate).


100. Id. at 718-19.

101. See, e.g., Liberal Mkt., Inc. v. Malone & Hyde, Inc. (In re Liberal Mkt.,

102. See, e.g., In re AllBrand Appliance & Television Co., 24 Bankr. 125 (Bankr.
S.D.N.Y. 1982).

103. See, e.g., In re Evergreen Valley Resort, Inc., 27 Bankr. 75 (Bankr. D. Maine
1983).

104. See, e.g., In re Original Auto Parts Distribs., Inc., 9 Bankr. 469 (Bankr.
S.D.N.Y. 1981) (adversary proceeding seeking to reclaim goods under section 546(c)
defended by the creditors' committee; no discussion of the appropriateness of the
committee's standing).
claims under section 510(c) of the Code\textsuperscript{105} and petition for the marshalling of assets.\textsuperscript{106}

Other courts have found that a committee's right to bring actions in its own name is rooted not in section 1103(c)(5), but rather in section 1109(b),\textsuperscript{107} which provides: "A party in interest, including . . . a creditors' committee . . . may raise and may appear and be heard on any issue in a case under this chapter."\textsuperscript{108} In analyzing section 1109(b), courts have sharply disagreed over whether the term "case" includes "proceedings" instituted under the Code.

In finding a committee has standing to seek recovery of preferences and allegedly diverted assets, United States Bankruptcy Judge Babitt of the Southern District of New York in \textit{Official Committee of Unsecured Creditors of Joyanna Holitogs, Inc. v. I. Hyman Corp. (In re Joyanna Holitogs, Inc.)},\textsuperscript{109} described a committee's rights under section 1109(b) as follows:

Section 1109(b) continues the broad concept, carried over from the 1898 Act, of the broad right to be heard in order to insure that the dark corners of commerce are illuminated. A general right to be heard would be an empty grant unless those who have such right are also given the right to do something where those who should will not. In short, the right to be heard given the creditors' committee, includes the right to sue where a trustee or debtor in possession will not. To hold otherwise would frustrate Con-


\textsuperscript{107} Although not involving the issue of standing in an adversary proceeding, the rights of a committee under section 1109(b) were found to include moving for rejection of a collective bargaining agreement under section 365 of the Code in \textit{In re Parrot Packing Co.}, BANKR. L. REP. (CCH) ¶ 69,372 (N.D. Ind. 1983). There, the debtor would not move to reject the collective bargaining agreement because of fear that such rejection would constitute an unfair labor practice under the National Labor Relations Act. Although the debtor actually supported the committee's application to reject, the court found that the debtor's refusal to act was "unjustified." \textit{Id.} at 83,137.

\textsuperscript{108} 11 U.S.C. § 1109(b) (1982).

\textsuperscript{109} 21 Bankr. 323 (Bankr. S.D.N.Y. 1982).
gress' decades-old effort to limit a debtor's generosity with its assets.\footnote{110}{Id. at 326 (citation omitted).}

A contrary conclusion was reached by a bankruptcy court in Puerto Rico, in \textit{Segarra v. Banco Central Y Economias (In re Segarra)}.\footnote{111}{14 Bankr. 870 (Bankr. D.P.R. 1981).} There, the court held that the term "case," as used in section 1109(b), does not apply to adversary "proceedings." The court found that Congress did not intend to create new causes of action in favor of committees and, accordingly, dismissed the committee as a party plaintiff in an action seeking damages from a creditor bank for improper dealings.\footnote{112}{Id. at 878.}

Where a committee is found to have standing to commence an adversary proceeding, is it subject to the concomitant duty to do so? In \textit{In re Overmyer},\footnote{113}{30 Bankr. 123 (Bankr. S.D.N.Y. 1983).} a New York bankruptcy court pondered this question and concluded that a Chapter 11 trustee seeking to reopen the time to file a complaint objecting to the discharge in the separate Chapter 7 proceedings of the shareholders of the debtor, was not prejudiced by the committee's failure to commence the action. While the court ruled the committee had a right to commence suit, the committee was not burdened by the correlative duty to do so and its inaction therefore did not estop the trustee from doing so.\footnote{114}{Id. at 125.}

2. Standing to Intervene

A related question involves the right of a committee to intervene in a suit already commenced by the debtor in possession or the trustee. In \textit{Official Unsecured Creditors' Committee v. Michaels (In re Marin Motor Oil, Inc.)},\footnote{115}{689 F.2d 445 (3d Cir. 1982).} the Third
Circuit Court of Appeals found that "cases" under 1109(b) included adversary proceedings, and held that the committee had an "unqualified" right to intervene, particularly where the trustee was lackadaisical in his pursuit of the fraudulent conveyances at issue. The participation of committees envisioned by Congress under section 1109(b), concluded the court, went far beyond the *amicus curiae* status afforded the committee by the bankruptcy court.

The view that a committee has an unqualified right to intervene in adversary proceedings was questioned by Oklahoma Bankruptcy Judge Bohanon in *Kenan v. Federal Deposit Insurance Corp. (In re George Rodman, Inc.)*. There the court relied on the fact that Congress distinguished between "case" and "proceedings" at numerous points in Title 28 of the United States Code. In addition, said the court, the Bankruptcy Rules which became effective on August 1, 1983 also distinguish between intervention in a "case" (governed by Rule 2018) and intervention in adversary "proceedings" governed by Rule 7024, which applies Rule 24 of the Federal Rules of Civil Procedure. The right of a committee to intervene in an adversary proceeding, concluded Judge Bohanon, is not mandatory as suggested by *Marin*, but is instead permissive. The court permitted the committee to intervene in the preference action at issue.

3. Standing and the Attorney-Client Privilege

Even if a committee is found to have standing to sue or to intervene under either section 1103(c)(5) or section 1109(b), the lack of a privilege between the committee and its counsel may hamper its ability to do so effectively. In *In re Christian Life Center*, the United States Bankruptcy Court for the Northern District of California found that there was no attorney-client privilege between a committee

116. *Id.* at 451.
119. *Id.* at 349-50.
120. *Id.* at 349.
121. *Id.* at 351.
and its lawyer. Although a trustee is a "mover and a shaker,"123 said the court, a committee has no power other than to consult and recommend, and should therefore make its activities known to other creditors.124 Christian Life was decided before many of the cases addressing the standing issue and involved allegations of illegal acts on the part of committee members. Nonetheless, the decision may impair the effectiveness of an active creditors' committee and its counsel if it is followed in other jurisdictions.

D. Reimbursement of Committee Expenses

Another frequently litigated issue is the right of committee members to seek reimbursement of expenses incurred in connection with a case. Section 503(b)(3)(D) provides that only committees other than those appointed pursuant to section 1102125 are entitled to the allowance of an administrative expense priority for out-of-pocket costs incurred in connection with fulfilling committee functions. The section also authorizes the reimbursement of expenses incurred by individual creditors who make a "substantial contribution" to a case. While acknowledging a probable decline in qualified members willing to serve on section 1102 committees if reimbursement of expenses is denied, which in turn impacts upon the entire Chapter 11 process, a majority of courts have nonetheless felt compelled to deny reimbursement, citing lack of authority to do otherwise.126

A few cases, however, have found expenses to be reimbursable. Relying on the prior Bankruptcy Rule of Procedure 11-29,127 which specifically permitted reimbursement of committee members' expenses, the United States Bankruptcy Court for the District of Minnesota allowed reimbursement in In re Fireside Office Supply, Inc.128 Section

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123. Id. at 37.
124. Id.
125. Committees appointed pursuant to 11 U.S.C. § 1102 (1982) include committees of equity security holders and creditors other than those represented by the official committee of unsecured creditors. See supra text accompanying notes 52-63.
503(b), said the court, is not comprehensive and exclusive, and therefore, there was no conflict between Rule 11-29 and section 503(b).\footnote{129} Since this decision was rendered, Rule 11-29 has been superseded by the new Bankruptcy Rules, which became effective on August 1, 1983.\footnote{130}

Taking a different tack, a Colorado bankruptcy court in \textit{In re Grynberg}\footnote{131} relied on that portion of section 503(b)(3)(D) which permits individual creditors, rather than committees, to be reimbursed if they make a "substantial contribution" to a case, and awarded reimbursement to individual committee members.\footnote{132} The court qualified its decision, however, by pointing out that simple appointment to a committee will not entitle a member to reimbursement. In addition, there must be a meaningful participation in the administration of the case, participation in the creation of a plan, or in the achievement of a plan's confirmation or in the denial thereof, before reimbursement will be warranted.\footnote{133} Interestingly, most other courts applying the \textit{Grynberg} analysis have found that committee members who diligently performed their duties nevertheless did not necessarily make a "substantial contribution" warranting reimbursement of their expenses under section 503(b)(3)(D).\footnote{134}

A leading decision denying reimbursement of expenses

\begin{itemize}
\item \footnote{129} \textit{Id.} at 45. \textit{Accord In re Pennsylvania Tire & Rubber Co.,} 25 Bankr. 18 (Bankr. N.D. Ohio 1982); \textit{In re American Strevell, Inc.,} No. 81-03652 (Bankr. D. Utah Dec. 11, 1981).
\item \footnote{130} The Bankruptcy Rules were promulgated pursuant to 28 U.S.C. § 2075 (Supp. III 1979).
\item \footnote{131} 19 Bankr. 621 (Bankr. D. Colo. 1982).
\item \footnote{132} \textit{Id.} at 622, 624.
\item \footnote{133} \textit{Id.} at 623.
\item \footnote{134} While one court has followed \textit{Grynberg} and allowed compensation to committee members, see \textit{In re GHR Energy Corp.,} 35 Bankr. 539 (Bankr. D. Mass 1983), most other courts have not. \textit{See, e.g., In re Farm Bureau Services, Inc.,} 32 Bankr. 69, 71 (Bankr. E.D. Mich. 1982) (court applied the \textit{Grynberg} analysis but denied reimbursement to committee members; committee members, said the court, are like parties to an "ordinary lawsuit contributing time and assistance to counsel, which expenses cannot be compensated."\textsuperscript{39}). \textit{Compare In re Lyons Mach. Co.,} 28 Bankr. 600 (Bankr. E.D. Ark. 1983) (reimbursement denied even though the plan paid all secured and unsecured claims in full) with \textit{In re Interstate Restaurant Sys., Inc.,} 32 Bankr. 103 (Bankr. S.D. Fla. 1983) (court made clear that only professional persons employed by committees were entitled to fees (as opposed to reimbursement of expenses) and denied a committee's request for compensation of the chairman and secretary).
to committee members is *In re Major Dynamics, Inc.*, where the bankruptcy court found that Rule 11-29 was in conflict with section 503(b)(3)(D), which clearly denied reimbursement to section 1102 committees, and was therefore inapplicable. Additionally, because the Code specifically denies the reimbursement of expenses to committees, it would be anomalous, said the court, to permit individual committee members to be reimbursed when the committee itself was not so entitled. The court noted that a Technical Amendments Act was then pending in Congress which would specifically authorize reimbursement of committee expenses. To date, however, this legislation has not been enacted.

One commentator has suggested that newly promulgated Bankruptcy Rule 2016(a), which deals with the application for compensation or reimbursement, should end the controversy. The Rule itself, however, does not specifically make reference to a creditors' committee, although the Advisory Committee Note suggests that reimbursement of a committee's expenses was intended to be covered. Until Congress enacts corrective legislation, or courts construe Rule 2016(a) to permit reimbursement of committee members' expenses, counsel should seek an order from the court clarifying committee members' right to reimbursement at the outset of the case.

136. Id. at 280.
137. Id. A similar amendment to section 503(b) was also included in the Bankruptcy Court and Federal Judgeship Act of 1983, S. 1013, 98th Cong., 1st Sess. 0642 (1983).
139. The Advisory Committee Note to Bankruptcy Rule 2016(a) reads, in pertinent part, as follows: "Subdivision (a) includes within its provisions a committee, member thereof, agent, attorney or accountant for the committee when compensation or reimbursement of expenses is sought from the estate." BANKR. R.P. 2016 advisory committee note.
E. Duties and Potential Liability of Committee Members

1. The Standard of Care: Fiduciary Responsibility

Members of a creditors' committee have a fiduciary duty to the holders of the class of claims or interests they represent. Members of a creditors' committee have a fiduciary duty to the holders of the class of claims or interests they represent. They must pursue their statutory function for the benefit of their constituency with an undivided loyalty. Because of this absolute requirement, some courts have refused to appoint overlapping committees, and others have declined to approve the selection of the same counsel for different committees in related cases. The potential for a conflict of interest is to be scrupulously avoided, even if there is no actual conflict at the time of the initial appointment or retention.

As a fiduciary, a committee member must not use his position to further his own interests at the expense of other creditors. Where a committee member abuses this trust by attempting to further his own interests, courts will not hesitate to impose sanctions. Illustrative is Johns-Manville Sales Corp. v. Doan (In re Johns-Manville Corp.), where a member of the Asbestos Committee, who was also an attorney, continued a prepetition lawsuit against the debtor on behalf of a private client. The bankruptcy court first condemned the creditor's attempts to advance prepetition claims postpetition without first securing relief from the automatic stay and then commented at length upon the nature of a committee member's fiduciary duty:


145. Id. at 647.

146. Id. at 919 (Bankr. S.D.N.Y. 1983).

147. The automatic stay, imposed by 11 U.S.C. § 362 (1982), stays inter alia acts to obtain property of the estate or from the estate.
In the case of reorganization committees, these fiduciary duties are crucial because of the importance of committees. Reorganization committees are the primary negotiating bodies for the plan of reorganization. They represent those classes of creditors from which they are selected. They also provide supervision of the debtor and execute an oversight function in protecting their constituent’s interests. . . .

Accordingly, the individuals constituting a committee should be honest, loyal, trustworthy and without conflicting interests, and with undivided loyalty and allegiance to their constituents. . . . Conflicts of interest on the part of representative persons or committees are thus not be [sic] tolerated. . . . [W]here a committee representative or agent seeks to represent or advance the interest of an individual member of a competing class of creditors or various interests or groups whose purposes and desires are dissimilar, this fiduciary is in breach of his duty of loyal and disinterested service.148

The court concluded that the committee member misused confidential committee information in furthering a private cause. The court stated that this abuse constituted a punishable breach of his fiduciary duty and fined the attorney and his law firm the amount of compensatory damages caused by their conduct, not to exceed $5,000.149

Surprisingly, there are no reported decisions under the Code imposing liability on committees or their members for failure to participate actively in the reorganization proceedings by exercising the powers given to them under the Code. Perhaps the same sense of hopelessness which may cause a committee not to act prevents creditors from considering whether the committee has properly represented them. It may also be difficult to prove damages since establishing that the committee failed to fulfill its fiduciary responsibilities

149. Id. at 926. See also In re National Equip. & Mold Corp., 33 Bankr. 574 (Bankr. N.D. Ohio 1983) (a union member of the priority creditors’ committee petitioned the court to order the debtor, at estate expense, to retract certain adverse statements made about the union prepetition; the court refused, chastising the union for attempting to use its committee membership to further personal interests); Foodservice Corp. v. Flagstaff Food Serv. Co. (In re Flagstaff), 9 COLLIER BANKR. CAS. 2d (MB) 9, 19 n.14 (Bankr. S.D.N.Y. 1981) (court questioned a committee’s attempt to seek reclamation for some, but not all, unsecured creditors).
may not in itself demonstrate that a better result would have been achieved if it had done so.

On the other hand, after years of relatively little litigation by private claimants against the trustees of retirement plans under ERISA, recently many actions have been commenced. The reason for the delay may have been the complexity of ERISA and the concomitant education period during which claimants and their counsel have become aware of their rights. Similarly, it is possible there will be an increased awareness among creditors about the responsibilities of committees which represent them in Chapter 11 proceedings and resulting claims against inactive committee members. It is the opinion of the authors that there are instances where the pursuit of such claims would be appropriate.

2. Securities Law Liability

As stated above, one of the committee's duties under section 1103(b)(3) is to participate in the formulation of a plan of reorganization. A committee may join with another party in proposing a plan, or propose a plan of its own upon the expiration or termination of the debtor's exclusive period to file a plan. Prior to seeking acceptances, the proponent of a plan must prepare a written disclosure statement containing "adequate information" about the plan which must be approved by the court. Upon approval of the disclosure statement, a person who solicits acceptances in good faith is absolved from any liability arising from any state or federal securities laws, including federal antifraud provisions which impose absolute liability upon a seller of securities who makes materially misleading statements, or who fails to state a material fact in connection with such sale. A committee which participates in the proposal of a plan of reorganization and complies with the Bankruptcy Code is

151. Under 11 U.S.C. § 1121 (1982), only the debtor may file a plan during the first 120 days after the entry of the order for relief, unless the court orders a shorter period upon a showing of cause.
153. Id. § 1125(e).
protected from securities law liability. However, the committee may not be protected if it knowingly prepares, or participates in the preparation of, a disclosure statement which is misleading or incomplete. In this case the solicitation of the plan has not been in good faith.\textsuperscript{155}

Section 1125(e) is the only section of the Code which expressly provides protection to committees from liability arising out of bankruptcy proceedings. Questions about the standard of care and about the liability of committees if that standard of care is not met are otherwise left unanswered by the Code and by available case authority.

3. Tax Liability

Committees often serve as agents for the purposes of distributing dividends to be received by their constituents pursuant to a plan. If a distribution is to be delayed pending objection to certain claims interest may be earned on the funds prior to such distribution. In this respect a question arises as to whether the committee must file tax returns and pay tax on the interest earned? While there is very little authority on this question, one case suggests that the answer is no. In\textit{In re Alan Wood Steel Co.},\textsuperscript{156} the Bankruptcy Court for the Eastern District of Pennsylvania ruled that a trustee, acting as disbursing agent of monies received pursuant to a Chapter XI plan under the prior Bankruptcy Act, was not required to file state or federal tax returns or pay tax on the $300,000 of interest income earned. The court reasoned that because the money held was actually the property of the class of creditors who were ultimately entitled to receive it, the interest income was that of the creditors and not of the agent. Additionally, because Congress failed to include disbursing agents in that section of the Internal Revenue

\textsuperscript{155} 11 U.S.C. § 1126(b) (1982). The Code does not address the standard of conduct for parties who solicit against acceptance of a plan. A committee may elect to vigorously oppose a plan and solicit rejections. In so doing, it may run the risk of having the rejections solicited disallowed because they were not solicited in compliance with section 1126(e) of the Code. \textit{Collier} suggests that a plan opponent seek a court order permitting solicitation of rejections to be made on the basis of the proponent's disclosure statement or ask the court to stay the solicitation of acceptances to permit the preparation of any additional disclosure materials which may be required. \textit{Collier, supra} note 13, at § 1125.03[7].

\textsuperscript{156} 7 Bankr. 697 (Bankr. E.D. Pa. 1980).
Code\textsuperscript{157} which requires receivers and trustees to file returns, the court ruled that there was no obligation to file returns.\textsuperscript{158}

There have, however, been no decisions regarding this question under the Bankruptcy Code. Accordingly, because of the lack of authority under the Code or the Bankruptcy Tax Act of 1980, committees which separately or jointly propose plans and which act as disbursing agents should take the precaution of clarifying their potential tax liability in advance pursuant to section 1146(d) of the Code.\textsuperscript{159}

**IV. DYNAMICS OF A CREDITORS' COMMITTEE**

**A. The Initial Decision to Serve on a Committee**

Although frequently avoided as an unwanted burden, service on a creditors' committee should be viewed as an opportunity. By actively participating as a committee member in the reorganization process, a creditor will have direct input into the manner and magnitude of the recoupment of a claim which may constitute a significant asset. Additionally, as a committee member, the creditor can directly facilitate the revitalization of what might be a valuable customer. Committee service may also suggest ways the creditor can improve its own internal procedures to minimize its future exposure as a creditor. It may also suggest possible revisions in its operations to avoid making the financial and operational mistakes of the debtor.

Reluctance to serve on creditors' committees may stem in part from prior experiences with inactive or ineffectual committees.\textsuperscript{160} However, committees can play a very active part

\textsuperscript{157} 26 U.S.C. § 6012(b) (1979).

\textsuperscript{158} The court also concluded that the agent was absolved from filing information returns under 26 U.S.C. § 6049 (1982) because the disbursing agent was actually an agent of the United States Bankruptcy Court and therefore outside the scope of the section. However, this section has been amended. Effective January 1, 1983, governmental units are no longer absolved from the requirement of filing information returns. Although there have been no reported decisions on point, this presumably includes the Bankruptcy Court, and the reasoning of Alan Wood Steel, 7 Bankr. at 702, regarding the duty to file information returns is no longer applicable.

\textsuperscript{159} 11 U.S.C. § 1146(d) (1982) permits the court to authorize a proponent of a plan to request an advance legal determination of state or federal tax liability related to a plan.

\textsuperscript{160} See LoPucki, The Debtor in Full Control - Systems Failure Under Chapter 11 of the Bankruptcy Code? (Second Installment), 57 AM. BANKR. L.J. 247, 250 (1983), a
in successful Chapter 11 reorganization and, in so doing, precisely fill the supervisory role that Congress designed for them.\textsuperscript{161}

B. Internal Procedures

Although the factors that help committees to achieve success are somewhat elusive, several elements seem to be common to successful committees. One of the most significant is internal structure and procedures. A committee must organize itself internally before it can act effectively. The committee should, for example, elect officers, including, at a minimum, a chairman and a secretary. The chairman should be a person willing to devote the time necessary to catalyze the committee, to make necessary decisions and to insure that decisions which are made are promptly implemented. This frequently entails contacting committee members between regular meetings to discuss and secure votes upon questions which may arise. Although size of claim may be one criterion for the selection of a chairman, a better qualification is past experience with bankruptcy reorganizations or out of court workouts.

An effective committee secretary also contributes to the overall success of a committee. The secretary should handle all administrative work of a committee,\textsuperscript{162} such as mailing notices to creditors, keeping and disseminating minutes of meetings and preparing committee reports. While in smaller cases these functions may be performed by a creditor, in larger cases it may be desirable to retain an outside party who can devote the necessary time to fulfill this role. It may be possible to retain employees of trade associations or other related groups which may have word processing or data processing capabilities as well.

\begin{itemize}
\item study which examined certain cases filed in the first year following the effective date of the Bankruptcy Code and which concluded, among other things, that creditors' committees were generally ineffective.
\item Comparing the Code to the prior Bankruptcy Act, committees, especially the unsecured creditors' committee, replace the court as the chief overseer of a debtor's activities. See generally Trost, Business Reorganizations Under Chapter 11 of the New Bankruptcy Code, 34 Bus. Law. 1309 (1979).
\item See In re Barsky, 17 Bankr. 396 (Bankr. E.D. Pa. 1982), where a committee counsel was denied compensation for work which should have been performed by the committee secretary.
\end{itemize}
It is desirable for a committee to adopt bylaws similar to those adopted by a business corporation. These serve as ground rules for the committee's internal operations and should cover such subjects as appointment and duties of officers, appointment of alternate committee members, voting procedures, quorums and voting by proxy and the formation of subcommittees. The adoption of bylaws may prevent future disputes or confusion about the effectiveness of actions subsequently taken by a committee.

The efficiency of a creditors' or interest holders' committee can be greatly enhanced by the effective use of subcommittees. Subcommittees diffuse the overall workload of a committee and also permit the committee to address several issues at the same time. Examples of common subcommittees include those charged with evaluating the debtor's prepetition and postpetition financial condition, identifying and evaluating candidates to acquire the debtor or its assets, monitoring and recommending improvement in the debtor's operating procedures, negotiating the terms of a plan of reorganization or formulating the committee's plan, and identifying recoverable assets, such as preferences and other avoidable transfers.

163. Although much importance is placed on the committee's adversarial relationship with the debtor, committees can provide valuable assistance as well. For example, a committee can greatly enhance a debtor's prospects for success by suggesting ways to improve internal operations. Frequently, the debtor can obtain goods or materials only on a C.O.D. basis, as opposed to dated terms, causing severe cash flow problems. The committee can sometimes alleviate this problem by informing creditors about their rights to an administrative claim for shipments made postpetition, pursuant to 11 U.S.C. § 503 (1982), or by working with the debtor to provide other assurances to shippers such as field warehousing or secured financing arrangements.

164. It is often useful to begin this process as early in a case as possible. A subcommittee can explore such concepts as conditional earnout provisions, the feasibility of sharing the proceeds of any postreorganization sale of the debtor's stock or assets or the receipt of securities in connection with the reorganization. Later, after further investigation of the debtor's operations is concluded, the committee should be in a position to formulate a minimum distribution percentage which can be recommended to creditors generally. By defining the minimum criteria to be included in an acceptable reorganization plan, the committee will be in a position to respond promptly to proposals made by the debtor or other parties, or to propose its own plan.

165. In *In re Gander Mountain, Inc.*, No. 80-03050 (Bankr. E.D. Wis. Dec. 9, 1980), the Unsecured Creditors' Committee identified and collected approximately $1.7 million in preferential transfers, thereby increasing the distribution to unsecured creditors from 55% to over 75%. As part of the collection effort, the committee af-
C. Resolution of Minor Conflicts of Interest

Frequently, creditors on committees may themselves have received preferences or other avoidable transfers. The member may understandably be concerned about a breach of its fiduciary duty to all creditors. Should, for example, the member disclose the fact of a potentially avoidable preference, perhaps to its disadvantage? If a member decides to contest the recovery, should its delegate resign? In large cases it is not unusual for large numbers of creditors to have received avoidable transfers. Resignation of their designees could cripple a committee's effectiveness at a crucial stage in the case. Although replacements may be ultimately appointed, the "start up" time required to become familiar with the committee's proceedings may be substantial.

Although there exists no universal solution to these questions, where simple avoidance actions, such as preferences, are involved, disruption of committee activities can be avoided by a discussion early in the case of the possibility of this situation arising. Assuming that a comprehensive investigation will be undertaken and a report produced, members may be told that disclosures which may be against their interest are neither necessary nor desired. If a subcommittee to investigate preferences is to be formed, its members might consist only of those who are confident they did not receive a preferential transfer. A member who did receive a questionable transfer should abstain from voting on matters relating to claims against it, and probably should excuse itself during the corresponding discussions relating to such claims.

These procedures could be formally incorporated into a conflict of interest provision included in the committee bylaws. While such procedures may be workable if the claim is relatively simple, such as a preference claim, if the dispute with the committee member involves matters other than routine avoidance actions, such as fraud, the committee member probably should resign.

forded recipients of preferences a limited opportunity to satisfy their liabilities by shipping goods, in this case, sporting equipment, to the debtor in an amount equal to the recipient's liability, but valued at the creditors' wholesale cost. Many creditors chose this option, taking advantage of their normal markup. This permitted the debtor to increase its inventory substantially without adversely affecting cash flow.
D. Committee Meetings

It is important for committees to meet periodically throughout the course of the case. Although much of the substantive work can be accomplished by subcommittees, the committee should periodically meet as a whole to discuss problems and make decisions based upon the recommendations of its subcommittees. It may not be essential to meet with absolute regularity, as the frequency of meetings may often be dictated by developments in a case. When meetings are held, however, it may be useful to structure them so that a portion is devoted to meeting with and questioning officers of the debtor, or the trustee, about developments in the case, with the remainder of the meeting held in executive session to take up committee business.

E. The Role of Committee Counsel

Finally, one of the most important elements of a successful committee is the participation of knowledgeable and experienced counsel. Frequently, committee members are businessmen whose expertise can be applied to maximum advantage only through the assistance of attorneys familiar with reorganization proceedings. In addition to advising the committee about its functions and duties, counsel can greatly assist it inasserting itself in the posturing and leveraging among competing interests that is frequently determinative of the outcome of the case.

V. Conclusion

Effective participation of committees of creditors and of other parties in interest in Chapter 11 proceedings should not be limited to the largest "national" cases. The Code gives committees broad powers which, when properly utilized, permit them to play a meaningful and sometimes dominant role in the outcome of cases of any size being administered under the Code. An active committee, represented by experienced, assertive and innovative counsel, can achieve the optimum result for creditors and assure that the members will not be called upon later to personally provide that which they should have obtained for those they represent in the Chapter 11 process.