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BANKRUPTCY-CORPORATE REORGANIZATION-POWER OF COURT TO ORDER INTERIM PAYMENTS WHILE PETITION IS PENDING UNDER CHAPTER X OF BANKRUPTCY ACT

William F. Snyder S.Ed.
University of Michigan Law School

BANKRUPTCY—CORPORATE REORGANIZATION—POWER OF COURT TO ORDER INTERIM PAYMENTS WHILE PETITION IS PENDING UNDER CHAPTER X OF BANKRUPTCY ACT—A petition for reorganization was filed, pursuant to Chapter X of the Chandler Act, October 3, 1947, which was adjudged on the same day to be in good faith and within the terms of the act. The corporation was clearly solvent, in the sense that its assets exceeded its liabilities, but needed financial adjustment to meet the principal on outstanding income notes due the follow-

ing June.[1] Thereafter, and before a plan was approved, the court entered an order directing the trustee of the debtor to pay 6% to the holders of the first mortgage bonds as an interim distribution to be applied against the principal amount due on such bonds. The debtor and holders of subordinate income notes appealed on the ground that this order amounted to partial liquidation unauthorized under Chapter X. *Held,* as these interim payments would not interfere with the general plan of reorganization, the court had power to order them. *In re Industrial Office Bldg. Corp.,* (3d Cir., 1949) 171 F. (2d) 890.

Beyond a doubt, an order calling for the payment of bonds before a plan has been approved is unique in a reorganization proceedings. The court could find only one other case under Chapter X in which such a procedure had been adopted.[2] There is also limited precedent for the use of such interim orders in railroad reorganization under Section 77,[3] and in equity receiverships.[4] Contrary authority appears even more limited.[5] On principle, the theories of liquidation and reorganization would seem inherently at odds, yet it is clear that complete separation of the two has never been achieved in practice.[6] This

[1] *Liabilities*:

Bonds	Principal	$1,954,000
	Interest	1,063,000
Unsecured Debts		10,000
Income Notes*	Principal	359,000
	Interest	401,000
Total		$3,787,000

* Principal due June 1, 1948. Interest accrued as of October 3,1947.

Cash on Hand:	
Oct. 3, 1947 (petition)	$293,000
March 31, 1948	432,000
April 30, 1948	448,000
Sept. 30, 1948 (estimate)	557,000
Net Monthly Income:	$ 20,000
Amount Needed for Alterations:	$250,000
Amount Disbursed:	
6% Distributed	$120,000
*10% Proposed	200,000

* This payment was held in abeyance pending the instant appeal.

[2] Application of Realty Associates Securities Corp., (D.C. N.Y. 1944) 58 F. Supp. 220. See also language in Central Hanover Bank & Trust Co. v. Philadelphia & Reading Coal & Iron Co., (C.C.A. 3d, 1938) 99 F. (2d) 642; In re Philadelphia & Reading Coal & Iron Co., (C.C.A. 3d, 1944) 141 F. (2d) 954.

[3] In re Central of Georgia Railway Co., (D.C. Ga. 1942) 42 F. Supp. 940; same case, 48 F. Supp. 445; Central Hanover Bank & Trust Co. v. Callaway, (C.C.A. 5th, 1943) 135 F. (2d) 592.

[4] Todd v. Lippincott, (C.C.A. 3rd, 1919) 258 F. 205.

[5] See FINLETTER, THE LAW OF BANKRUPTCY REORGANIZATION 363-373 (1939), where he apparently assumes the invalidity without any citations.

[6] Id. at 14, n. 14. In re Lorraine Castle Apartments Bldg. Corp., Inc., (C.C.A. 7th, 1945) 149 F. (2d) 55; Country Life Apartments, Inc. v. Buckley, (C.C.A. 2d, 1944) 145 F. (2d) 935; Cary, "Liquidation of Corporations in Bankruptcy Reorganization," 60 HARV. L. REV. 173 (1946).

amalgamation is expressly recognized in Sec. 116 (3) of the Chandler Act which allows the court to lease or sell debtor's assets before a plan is approved.[7] The instant order should be able to draw strength from the policy if not the terms of such a provision. It is often quite desirable that a court sitting in bankruptcy be able to exercise the flexible powers of equity.[8] Still it must be remembered that the elaborate machinery of Chapter X was designed to meet an actual evil, and courts should be reluctant to circumvent that procedural bulwark.[9] The principal case is really but one phase of the larger problem of paternalism against flexibility which was debated in connection with the adoption of present Chapter X.[10] The good sense of such an order, under the unusual financial structure of the present corporation, seems self-evident, but the danger of expanding such a practice cannot be overemphasized.

William F. Snyder, S.Ed.

[7] This section is adopted from subsection C (3½) of old §77B which was added by amendment in 1937. See H.R. REP. No. 914, 75th Cong., 1st sess. (1937).

[8] So held in Pepper v. Litton, 308 U.S. 295, 60 S.Ct. 238 (1939).

[9] For a summation of these safeguards see S.E.C. v. U.S. Realty and Improvement Co., 310 U.S. 434, 60 S.Ct. 1044 (1940).

[10] Cf. Swaine, "Democratization of Corporate Reorganizations," 38 COL. L. REV. 256 (1938) with Douglas, "Improvement in Federal Procedure for Corporate Reorganizations," 24 A.B.A.J. 875 (1938). See also Dodd, "The Securities and Exchange Commission's Reform Program for Bankruptcy Reorganizations," 38 COL. L. REV. 223 (1938).