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On Comparing Friendly Adjustment and Bankruptcy

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ON COMPARING "FRIENDLY ADJUSTMENT" AND BANKRUPTCY†

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The dissatisfaction in which our judicial machinery stands is such that any process of settlement labelled popularly "out of court" or technically "extra-legal" or "extra-judicial" has come to have a connotation synonymous with, if not perfection, at least unquestioned superiority. Because of court delays, cumbersome machinery, questionable attorney methods, incompetence of judges, and the expense incident to judicial settlements, conciliation, arbitration and extra-judicial settlements are assuming positions of undeniable importance in all branches of the law.[1] It has recently attained prominence in the field of insolvency liquidation. Here, the characteristic phrase employed for the particular substitution for court machinery is "friendly adjustment."

This article is intended to be an examination of some of the claims of superiority of the "friendly adjustment" system over the bankruptcy system in the matter of liquidating insolvent estates. Mr. Billig in his recent excellent articles expounding such claims,[2] has defined "friendly adjustment" as being "that type of settlement or liquidation effected through the co-operation of the insolvent debtor with his creditors."[3] This would, however, seem to be more of a hope and an enthusiastic conclusion than a definition. In theory, it might equally be applicable to that type of liquidation effected under the Federal Bankruptcy Act.[4] There can be many types of "friendly adjustment." Any settlement without court intervention may be so termed.

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[1]Lauer, *Conciliation—A Cure For The Law's Delay*, (1928) 136 ANN. OF THE AM. ACADEMY OF POL. AND SOC. SCIENCE 54.

[2]Billig, *What Price Bankruptcy: A Plea for "Friendly Adjustment"* (1929) 14 CORNELL LAW QUARTERLY 413; Billig, *Extra Judicial Administration of Insolvent Estates: A Study of Recent Cases* (1930) 78 U. OF PA. L. REV. 293.

[3]Billig, *Extra-Judicial Administration of Insolvent Estates, supra* note 2, at 295.

[4]"The present Bankruptcy Act is founded on the democratic principle of creditors' suffrage—it is the creditors who elect the trustee to administer the estate." 2 REMINGTON, BANKRUPTCY (1923 ed.) §1097.

The "Friendly Adjustment" considered here is that type of extra-legal insolvent estate settlement or liquidation which is carried out by means of adjustment bureaus approved by and operated under a business men's association called the National Association of Credit Men. This method, the most outstanding of any of the extra-legal settlements that fall under the head of "friendly adjustment," briefly, is as follows: When the case is once accepted by the bureau, the liquidation is carried out by means of an assignment for the benefit of creditors or deed of trust, made to the bureau liquidator as trustee. The trust deed invariably empowers the trustee to sell the assets of the estate, and distribute the proceeds to creditors after deducting the expenses of administration.[5] These expenses normally consist of approximately a 10% fee of the net assets realized. Other features of the plan will subsequently appear as incident to the discussion.

It is proposed neither to make a "defense" of, nor an "attack" upon either system, although, as the nature of the previous discussion has been only to select and emphasize the defects in bankruptcy, completing the picture would almost necessarily require counteractive treatment. It is merely intended herein to illustrate what is considered to be the inaccuracy of some of the contentions that have been presented for each pro and con, to illustrate the necessity of tempering other arguments and to offer still others unmentioned. By thus presenting a clearer comparison of the two systems, it is hoped to demonstrate wherein lies the superiority of one over the other, and what the word "superiority" in this regard should be taken to mean.

It will, of course, be impossible to consider fully all of the phases wherein these systems are held to be respectively effective, since this would practically require a complete diagnosis of each. The task obviously would be stupendous. Hence, only a few of the major, outstanding problems that already have been treated will be discussed, and with an eye only to comparisons. In general, these will be treated in the scheme in which the problems have already been presented by Mr. Billig: (1) The merchandising or marketing problem, namely, the methods of best reducing the assets to cash; (2) Creditor co-operation; (3) High cost of administration and consequent low returns to creditors.

"The present law goes further than any Bankruptcy statute either here or elsewhere in giving creditors the right to choose the trustees." 2 COLLIER, BANKRUPTCY (13th ed. 1923) 1018.

[5]For a detailed description of these bureaus and their methods of handling a case, see Billig, *What Price Bankruptcy: A Plea for "Friendly Adjustment"*, *supra* note 2, at 425. Also see *In Defense of the Nation's Receivables* (1927) BULL. NAT. ASS'N OF CREDIT MEN.

I. Problem of Marketing the Assets

A. *Legal* vs. *Economic*

The underlying objection to the present bankruptcy administration of insolvent estates is that it is said to be treated as essentially a legal and not an economic function; whereas friendly adjustment is allegedly founded upon the hypothesis that "the disposition of an insolvent debtor is a business and not a legal function."[6] The friendly adjustment type of liquidation need adhere to no rigid outline of procedure. Sales and distribution are accomplished with regard only for rules of business acumen. Quick sales are effected. Creditors are constantly kept informed while the estate is speedily liquidated. The court and its legalities, petitions,[7] and lawyers are thereby eliminated,[8] the liquidation being regarded as essentially a business function.

In innumerable ways are the above considerations true.[9] An organization with a large office force of constantly employed workers should be able to liquidate a great number of cases efficiently and cheaply. The work could be handled on a large scale, with business economies that can not be taken advantage of by the "single case" bankruptcy machinery.[10] Where it is possible so to do it, failure to adjust the

[6]Billig, *What Price Bankruptcy: A Plea for Friendly Adjustment, supra* note 2, at 426.

[7]See Report of the Joint Committee of the Association of the Bar of the City of New York, The New York County Lawyer's Ass'n and the Bronx County Bar Ass'n, In the Matter of an Inquiry Into the Administration of Bankrupts' Estates (1930) 151.

[8]"Legal fees are the most important single item of bankruptcy expense." *Ibid.* 29.

[9]"Administration has become not only a burden to the courts, but legalistic, long drawn out... It has developed on the part of business men an attitude towards the bankruptcy system of distrust and even disgust. Increasingly, in this District, as in other sections of the country, they are turning to other methods of liquidating insolvent estates." *Ibid.* 7.

"The administration of estates should be placed upon a business-like basis." *Ibid.* 12.

Rosenberg, *Put The Bankruptcy Business In The Hands of Experts,* Forbes Mag., April 1, 1929, at 14.

[10]Report by the Committee on Bankruptcy Reform, The Merchants' Ass'n of New York, (1924) 44.

Report, In the Matter of an Inquiry, etc., *supra* note 7, at 84:

"The appointment of a special receiver for each bankruptcy is about as modern a method of administering a bankrupt's estate as it would be to appoint a special attorney for the prosecution of each crime....It is a most expensive method of administering bankrupt estates, for, if ordinary business principles of organization and administration were applied, the first effort at economy would be in the direction of consolidating proceedings, reducing overhead, and departmentalizing the work."

liquidating machinery so as to gain such advantages is obviously wasteful. Thus, this phase of the problem also suitably finds a place under the third heading "High Cost of Administration", and the discussion here presented should also there be considered equally applicable.

The "business" technique, however, is one that is more than likely not to lend itself to the conditions and problems actually encountered. This is so because there are a vast number of considerations other than that of an efficient business mill turning out hundreds of cases. As a broad statement, it is difficult to understand how the administration of any technical, statutory enactment involves solely "business" rather than "legal" methods, if a distinction must be made between the two.[11] Few, it would seem, in this present day would dispute either the actual business necessity of a national bankruptcy act of some sort. The National Association of Credit Men itself was far-sighted enough to be among the original advocates of a bankruptcy statute.[12] Where any statutory enactment is involved, it would appear

[11]Might it not seem that "business" and "law" are so intimately bound together in this connection that it is extremely difficult to draw a line between the two? The so-called "legalistic" theory, calling for petitions to the court by the receiver and trustee to do such acts as "selling real estate at auction, redeeming property from a lien, selling property subject to a lien, or selling perishable property." (Billig, *Extra-Judicial Administration of Insolvent Estates, supra* note 2, at 27) is mainly for the purpose of allowing creditors to be heard so that they may handle these matters according to their own business-like judgment and methods.

The statement has also been made that "the services of these lawyers cannot be dispensed with under the prevailing system." Billig, *What Price Bankruptcy: A Plea for "Friendly Adjustment", supra* note 2, at 420. This is not wholly accurate. In the Yale School of Law Study of Bankruptcy cases in the District of New Jersey, it was found that out of 100 cases picked at random, in 10 the trustee had no attorney, in 4 the receiver had no attorney, and in 3, neither had attorneys. This was probably aided by the fact that such receivers or trustees were attorneys themselves. In like manner, it has been suggested that the "official receiver" should preferably consist of a lawyer and legal staff, because of the legal services and knowledge required at every turn of the receiver's routine duties. See Report, THE MERCHANTS' ASS'N OF NEW YORK, *supra* note 10, at 46.

In New York City, however, "an examination which we made of 854 cases prior to the appointment of the Irving Trust Co. disclosed that in every one of them, there was an attorney for the receiver". Report, IN THE MATTER OF AN INQUIRY, ETC., *supra* note 7, at 108. At present, however, the Irving Trust Co. does not employ attorneys in every case.

[12]Billig, *Extra-Judicial Administration of Insolvent Estates, supra* note 2, at 317.

to be axiomatic that the lawyer's presence is not superfluous, if not absolutely necessary. Words must be interpreted, "legislative intent" must be determined, a body of precedents develop that must be known or be able to be discovered,—the innumerable situations calling for the laywer's and the court's services where any statute is involved are too obvious to require further elaboration.[13]

But especially in the administration of a statute such as the Bankruptcy Act something in the nature of a "legal" technique would seem peculiarly useful. The collapse of a business structure or of an individual's affairs invariably leaves a tangle with which the lawyer can best cope. There is very often more than the simple matter of marshalling the assets, selling them and distributing the proceeds to creditors. After first solving the often difficult problem of what comprises the estate,[14] encumbrances which must be removed offer legal stumbling blocks. Discovering the number of liens, mortgages, conditional sale agreements, and examining their effect and validity often present bewildering situations. A "business man" would naturally be lost in the maze of entanglements commonly encountered in the administration of this particular type of estate.[15] In the further problem of the fraudulent failure, it would seem that the law with its definitions, and the lawyer with his knowledge and interpretations of the law are both necessary. And as would be expected, friendly adjustment by admission is neither capable nor desirous of handling a so-called "fraudulent" failure.[16] In support of the contention that only a negligible number of bankruptcies falls into this category, the average failure being one of mere business inefficiency,[17] Bradstreet's figures as to the causes of business failures are offered in evidence,[18] and the common, inherent feeling is invoked that most men, including

[13]See report, IN THE MATTER OF AN INQUIRY, ETC., *supra* note 7, at 12, 25.

[14]Bonbright and Pickett, *Valuation to Determine Solvency Under The Bankruptcy Act*, (1929) 20 COL. L. REV. 582, 596.

[15]The situation would appear somewhat comparable to that encountered in the administration of decedents' estates with its attendant collapse of affairs, in which statutory enactments, and therefore court administration and lawyers' services are necessary.

[16]Billig, *Extra-Judicial Administration of Insolvent Estates, supra* note 2, at 296.

[17]*Ibid.* 297; Billig, *What Price Bankruptcy: A Plea for "Friendly Adjustment", supra* note 2, at 417.

[18]Billig, *Extra-Judicial Administration of Insolvent Estates, supra* note 2, at 297, n. 10; Billig, *What Price Bankruptcy: A Plea for "Friendly Adjustment", supra* note 2, at 417, n. 22 (a).

business men, are honest. But such an analysis of the causes of failures,[19] placing as it does in definite, cut-and-dried categories every failure, attributing to each, one specific "cause", like pegs fitting exactly into holes, cannot be accepted as of significant value. The complicated causes for business failures cannot be so reduced to pigeon-holed conclusions, for the factors entering into any given case are innumerable. The Yale School of Law investigation finds them social, medical, psychological and economic.[20] Furthermore, the mere cursory reading of the records of a large number of closed bankruptcy cases leaves one with the firm conviction that affirmative "fraud" as a cause enters into many more cases than have been so classified.[21] And still further investigation discloses that even though the major, outstanding "cause" of large numbers of cases cannot be attributed to the one word "fraud", nevertheless situations approaching the "illegal" and "fraudulent" crop up everywhere in such cases. A bankrupt who has been rendered such by reason of a motor vehicle acci-

[19]"The Bradstreet report on causes of business failures in the United States during 1928 states that, out of 20,373 such failures, 6396 were caused by the incompetence of the insolvent; 7290 resulted from his lack of capital; and such specific conditions as disaster, war and floods were responsible for 3613 others. Only 544 of the failures reported were caused by fraudulent conduct on the part of the insolvent. The remainder were brought about by inexperience, unwise credits, neglect of business affairs and competition." Billig, *Extra-Judicial Administration of Insolvent Estates, supra* note 2, at 297.

[20]The typical "cause" of many failures would have to be explained in terms similar to these: "...a combination of rent too high for the volume of business reasonably handled by a business man of the particular type studied with an unusual amount of family illness, the condition being aggravated by a lack of caution on the part of certain large creditors in extending credit. The whole combination of circumstances, however, led to an easily avertable insolvency if the debtor had not finally become involved with 'loan shark' agencies."

See Clark, Douglas & Thomas, *The Business Failures Project—A Problem in Methodology* (1930) 39 YALE L. J. 1013.

[21]This mainly because of the large numbers of no-asset cases which slip by with no or inadequate investigations, so that the causes of these failures are never made clear, though many show almost unmistakable signs of fraud. Creditors are unwilling to go to the expense of conducting private investigations which they feel they should not bear, or which would be exceedingly difficult to prove, thereby involving larger losses than already suffered.

The author examined over 1,000 cases closed during the fiscal year 1928-1929 in New Jersey.

Also, see Wisehart, *Have You The Right To Be In Business?*, Am. Mag., Aug. 1930, at 27, quoting Federal Judge Clark of the New Jersey District...."a large majority of those who are benefiting by the Bankruptcy Act are incompetent or unethical business experimenters."

dent and a resulting judgment for negligence may attempt to conceal assets. Another whose plight was caused by large medical bills resulting from unprecedented illness may attempt to "take care" of a few of his friends, relatives, and friendly creditors before filing his petition. The situations are innumerable. In other words, fraud may play an important part in bankruptcies not set in motion with fraudulent intent. When the rigorous procedure of the Bankruptcy Act does not seem completely capable of coping with these situations there should at least be hesitancy in discarding whatever protection it might be able to furnish.

The friendly adjustment scheme must therefore be prepared to deal with the fraudulent cases if it seeks to cover the ground adequately. Even if it refuses to deal with them it must face the problem "what is fraud?", *i.e.,* by what rule of thumb is friendly adjustment to decide whether or not to accept the case. The formula offered is that when upon general examination, the debtor appears to be honest, willing to cooperate with his creditors, and to lay his traditional cards upon the proverbial table,[22] it is a case for friendly adjustment. Even assuming for the sake of the discussion that the differences between fraud and inefficiency are more than ethereal[23] (and to the average creditor who has shipped goods for which he has received no return payment, this difference is more apparent than real),[24] the test offered would still appear unsatisfactory. Who can attempt to say what is "honesty" or "fraud" *in vacuo?* Might not one creditor's conception be entirely different from that of another? Might not the bureau's standard be still another, considering the psychological, subconscious effect of the fee of at least 10%?[25] Does it not seem that the problem of "what is fraud?" in this connection can pursue only philosophical, speculative paths and reach inevitably the only concrete answer we have, *i.e.,* the product of human experience as exemplified in "the law"; that friendly adjustment, in its search of what is an "honest" bankrupt, should find itself forced to resort to the

[22]Billig, *What Price Bankruptcy: A Plea for "Friendly Adjustment", supra* note 2, at 430.

[23]Compare in tort law the disappearing distinctions for liability between negligent or affirmative misconduct, and "accidental" injuries.

[24]Likewise, in tort law, the person who is injured accidentally rather than intentionally or negligently.

[25]In Mr. Billig's excellent charts setting forth the results of certain cases liquidated by bureaus during 1926-1927, the average cost of administration appears to be 13.85% of the amounts realized. See Billig, *What Price Bankruptcy: A Plea for "Friendly Adjustment", supra* note 2, at 432, 433.

law's dictation of what shall or shall not be considered as "honest" dealings? In this instance, it can be found only in the Bankruptcy Act.

So far fraud and dishonesty have only been mentioned in relation to the bankrupt. But the Bankruptcy Act also provides creditors with protection against each other. The importance of such protection cannot be over-emphasized, yet there seems little in the friendly adjustment scheme to furnish it. Three sections of the Bankruptcy Act safeguard the rights of creditors *inter se*: Section 60 allows suit for the recovery of preferences to creditors within four months of the filing of the petition, and Sections 67 and 70 provide for the recovery by the trustee of fraudulent transfers in which creditors have participated. And in certain situations, especially where corporations are involved, it may be considered essential, either by state statute[26] or case law,[27] to refuse to countenance certain conduct upon the part of the creditor, though it be innocent and devoid of preferential intent.[28] In the interests of public policy, the frame of mind or conduct of the debtor, then, should not be the sole criterion as to the bureau's acceptance of a case. The *raison d'etre* of the Bankruptcy Act, it must also be remembered, is equality of distribution to creditors.[29]

The administration of any statute requires in innumerable ways the court and the lawyer. A bankruptcy act in particular, with its entangling problems, peculiarly necessitates the lawyer's services, and the problem of fraud and other allied considerations to which the nature of this subject especially finds itself susceptible, can best be solved by the law and the lawyer. These reasons indicate that one should be wary of wholly subscribing to the fundamental hypothesis of friendly adjustment, that "the disposition of insolvent estates is essentially a business, not a legal function."

B. *Realization of Assets*

The bankruptcy machinery is said to be unsatisfactory in reducing the debtor's assets to cash because of the frequent employment as

[26]N. Y. CONS. LAWS, c. 59 (STOCK CORP. LAW) §15. Under the Stock Corporation Law, a transfer may be declared void although the creditor had no reasonable cause to believe that any preference was being effected. (Amendment to the Law effective April 15th, 1929. N. Y. CONS. LAWS, c. 59 (Cum. Supp. 1930) §15.) Section 67 e of the Act is so construed as to give effect to local state law.

[27]Woods v. Metropolitan Nat. Bank, 126 Wash. 346, 218 Pac. 266 (1923), which accomplishes the same result by means of the "trust fund" theory of corporate assets.

[28](1929) 38 YALE L. J. 788.

[29]See 1 COLLIER, BANKRUPTCY (13th ed. 1923) 6.

receiver or trustee of a lawyer who is unskilled in business or merchandising.[30] In this important operation, the "business man" hypothesis does seem to have especial significance. Obviously, business men as a class can buy and sell merchandise better than attorneys as a class. Familiarity with bankruptcy practice, however, discloses the fact that the same men recur as bankruptcy officials so frequently that ample opportunity is presented them to become expert in merchandising. In some measure, also, these frequent appointments afford the bankruptcy machinery some of the advantages of the large scale methods above discussed.

Furthermore, although the picture of a permanent organization is not associated with bankruptcy,—to which have been applied the terms of "single case receiver" and "single case trustee",—the repeatedly appointed receiver or trustee may also have his regularly employed helpers. If they do not take the form of a "staff", nevertheless, skill obviously may be attained as a result of repeated operations. That lawyers receive these recurring appointments would appear to favor the susceptibility to becoming skilled. Lawyers are not at the lowest plane of intelligence.[31] Of course, not all officials fall into this repeatedly appointed, and therefore experienced class. Thousands are appointed once, or only rarely. These are usually ignorant of the necessary operations and the quality of their work is poor.[32] It cannot

[30]Billig, *Extra-Judicial Administration of Insolvent Estates, supra* note 2, at 298; Billig, *What Price Bankruptcy: A Plea for "Friendly Adjustment", supra* note 2, at 417.

[31]Joseph B. Jacobs, a Boston attorney, wrote us:

"Some of the worst fizzles in receiverships, both in equity and bankruptcy in this jurisdiction, have been the administration of business men as receivers."

Referee B. Loring Young of Boston, testified to the same effect. Report, IN THE MATTER OF AN INQUIRY, ETC., *supra* note 7, at 85.

"Business men apparently cannot generally be induced to serve, and where they have served, the experiment has generally proved unsatisfactory. Attorneys receive the bulk of appointments everywhere." *Ibid.* 106.

[32]See report, IN THE MATTER OF AN INQUIRY, ETC., *supra* note 7, at 17. Over half of the appointments in New York City from July, 1927 to January, 1929, were made in favor of those who received only one appointment. "Most of those appointed either had no training in liquidation work or were designated in so few cases that they never became really familiar with their more important duties. With but few exceptions they had neither the time nor the skill which the work required."

It should be remembered, however, that it is the *attorney* for the receiver and trustee that has generally come to the important liquidating officer. The former New York City condition was such that "The bulk of the Bankruptcy practice ...was concentrated in the hands of approximately 21 law firms." *Ibid* 4. In the

be claimed that the Bankruptcy situation is as satisfactory as that which would accrue from a large and steadily employed organization.[33] The actual, present conditions in bankruptcy, however, are not completely alien to the proposed situation.

The repeated appointment of the same persons to the positions of receiver and trustee, while it may result in the acquisition of marketing skill, has been declared to be a weakness and the system which leads to the odious "ring". Some consideration must now be given to this objection to the bankruptcy system. The word "ring" is employed in two ways. First, it applies to the group which secures for itself the offices and fees in the case. By favoritism with judges and referees, by solicitation of claims, by filing an involuntary petition or a petition for the appointment of a receiver, either of which invariably leads to the positions of attorney for the receiver and trustee,[34] control of the case is secured. Second, it also may apply to that group of auctioneers and henchman-buyers and bidders who stifle competition. These "rings" may intertwine or be identical. The latter is the more important in a consideration of the marketing problem.

The cry of "ring", fraud and dishonesty as a reason for avoiding bankruptcy and invoking friendly adjustment has frequently sounded.[35] It is a charge at times rightly made and with which bankruptcy has often been embarrassed. As a basis for the preference of friendly adjustment it is, of course, a just one. Where one system is administered by honest men, and a rival system by rogues and the dregs of a profession, no business man should patronize the latter.[36] But if the bank-

Yale New Jersey study, although complete analysis had as yet not been made, it was obvious that the great bulk of cases are liquidated by the same persons, who appear intermittently as receivers, trustees, or attorneys for the receiver or trustee.

[33]See report, THE MERCHANTS' ASS'N OF NEW YORK, *supra* note 10, at 36.

[34]Certain districts, New York included, have enacted a rule prohibiting the appointment of attorneys representing petitioning creditors or creditors petitioning for the appointment of a receiver from acting either as attorney for the receiver or trustee, unless specially authorized by the court. In New Jersey, however, out of 50 cases picked at random, in which there were these various offices, 49 showed the same attorneys for the receiver and trustee as appeared either for the petitioning creditors or petitioned for a receiver.

[35]Billig, *What Price Bankruptcy: A Plea for "Friendly Adjustment"*, *supra* note 2, at 413, 414, 415, 418, 422, 423, 424, 425, 427, 444, 445; Billig, *Extra-Judicial Administration of Insolvent Estates*, *supra* note 2, at 293, 294, 295, 300, 318, 319.

[36]Pope's oft-quoted lines from his *Essay on Man* should probably here be kept in mind:

"For forms of government let fools contest;
Whate'er is best administered is best:"

ruptcy system is, in certain localities saturated with dishonest practitioners who are the shame of the Bar this is not necessarily to be taken as such "evidence of flaws in the system itself",[37] as to make it unquestionably worthy only of being discarded. It may or it may not be.[38] It is primarily with such systematic faults and their alleged correction in friendly adjustment with which we can here be concerned.

Considering the repeated appointments to be evidence of a "ring", or asserting that the possibility of such "ring" formation is an inherent weakness in the system, may not always be just. It may be evidence of many other conditions—of an enlightened referee who wishes to have a trained group of men administer the cases assigned to him; of honest judges or referees who insist upon having themselves surrounded by men whom they feel they can trust and who are also honest; of the appointment of attorneys who know most about the case and who therefore are in position to give the most valuable and intelligent service.[39] To discard the bankruptcy system in favor of friendly adjustment for this reason is a ridiculous indictment of human nature, the Bench and the Bar.[40]

If there are rings in some localities there are other localities, where thousands upon thousands of bankruptcy cases are administered honestly.

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[37]Billig, *What Price Bankruptcy: A Plea for "Friendly Adjustment," supra* note 2, at 415.

[38]"The all-important fact is that the system was such as not only to facilitate, but to invite both inefficiency and corruption." Report, IN THE MATTER OF AN INQUIRY ETC., *supra* note 7, at 6.

"The administration cannot be improved except by a fundamental change in the statute itself." *Ibid.* 13.

But see Coles, *The Donovan Report, etc.,* (1930) 16 A. B. A. J. 431, in which Col. Donovan's failure to distinguish between faults of the law and faults of administration is commented upon.

[39]The Committee in the report, IN THE MATTER OF AN INQUIRY, ETC., *supra* note 7, at 34, recommends that "the rules concerning the retention of the same creditor's attorney or any attorney for the receiver or trustee be left to local regulation".

[40]See testimony of Referee Joseph B. Cheshire, Jr. of Raleigh, N. C. "which is typical of many others received from the smaller districts," *Ibid.* 204 "In this part of the country, we do not have a great many problems that confront the referees in the large cities of the East or Middle West. Our population is stable and native and we know everyone. I am personally acquainted, and have been for years, with 75% or more, of the lawyers who practice in bankruptcy matters....I also know a great many of the trustees personally and know all about them. I can usually get very high class trustees to accept cases, as a matter of public duty, where the compensation is totally inadequate for the work involved."

Also, as has been often pointed out, both the conditions of unskillfulness (which is more closely connected with the marketing problem) and dishonesty can largely be cured under the present Act by the repeated appointment as receiver of a large, reputable trust organization, the practice now adopted in the Southern District of New York. This is one of the recommendations made for bankruptcy by Mr. Billig,[41] but as it can be effected without an amendment to the Act, it is a suggestion that is not necessarily concerned with "evidence of flaws in the system itself". Whether or not the general idea is to be attributed to, or is to be taken as a lesson to be learned from friendly adjustment, it has the indorsement of many of those familiar with the situation.[42]

It is still difficult, however, to understand how any given method would entirely do away with the possibility of the "ring", as it is alleged friendly adjustment would accomplish. Honesty is not a quality that is peculiar to corporations or associations. Both friendly adjustment and bankruptcy, as is the case with any system, must work through individuals, who in turn must exercise discretion, make decisions, etc.[43] Of course, reputation for honesty is practically the sole assurance against "ring" work in any given case,[44] as it is in any other phase of law or business, and risks of dishonest favoritism in

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[41]Billig, *Extra-Judicial Administration of Insolvent Estates, supra* note 2, at 318.

[42]In the report, THE MERCHANTS' ASS'N. OF NEW YORK, *supra* note 10, Judge Learned Hand, Judge Knox, and Judge Manton among many attorneys and business men testified in favor of "Official Receivers" which is also the device employed in the English Act.

See also the report, IN THE MATTER OF AN INQUIRY, ETC., *supra* note 7, at 20, 116-121, endorsing the Irving Trust Co. idea

In this connection, it is interesting to note that one of the largest and most influential of the Friendly Adjustment bureaus is vigorously opposed to the recently adopted experiment in the Southern District of New York.

A minority of the Committee submitting the report, THE MERCHANTS' ASS'N. OF NEW YORK, *supra* note 10, dissented in part from the recommendations concerning official receivers.

[43]See Casey, *Corporate Administration Of The Bankruptcy Law* (1930) 15 COMM. LAW LEAGUE 292.

[44]"It (the scheme of Official Receivers) would work provided the pooling... would be sufficient to maintain a corps of really competent assistants. It is not the eight or ten people whom you make your Official Receivers; it is the character of the staff you have....They have to be paid, and be paid decently; it is purely a question of finance." Testimony of Miss Bertha Rembaugh in the report of the Commission on Bankruptcy Reform, MERCHANTS' ASS'N. OF NEW YORK, *supra* note 10, at 46.

appointments might be considerably lessened if such a commonly reputed, "honest" entity were repeatedly appointed. An individual, however, could also easily fulfill these requirements, but there is difficulty in finding individuals who would be willing to spend the required time on such comparatively unremunerative work. A wealthy corporation, however, might he willing to fill the role.[45] But it should be pointed out that though the use in bankruptcy of a large reputable corporation even satisfies some of the friendly adjustment critics, it would not *ipso facto* eliminate the "ring" a possibility to which *any* system is susceptible.

The "ring", then, it would seem, is a question of human frailty rather than of weakness in the system adopted, and it is not peculiar to bankruptcy. Equally as vicious "rings" may crop up as a product of the friendly adjustment system, nor is there any guarantee that its increased power and growth will not furnish similar problems with those of the bankruptcy named. The devices by which dishonesties may be veiled in a long standing system as bankruptcy are obviously greater than in the comparatively recent friendly adjustment system. If one system eliminates dishonesty and another is saturated with it, examination discloses that there is little that is inherently systematic to account for the difference, unless it be the elimination of lawyers. The officials of both are bonded. Both systems function upon a fee basis. Any allegations of difference appear to be mere platitudes.[46]

The solution for this whole problem of marketing assets, if there is any solution, would rather seem to be a complete discarding of the

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[45]The Irving Trust Co. in New York does not consider their venture to be of great financial potentiality. It was described to the author as "a social experiment". See the memorandum filed in the report, IN THE MATTER OF AN INQUIRY, ETC., *supra* note 7, at 10: "Stautory fees allowed in the small estates are so far exceeded by the cost of administration that the Trust Company has thus far found the business as a whole unprofitable, and may be constrained to abandon it. Up to July 1st, 1929, the average fees of the Trust Co. per case were $198.59, the average cost per case $407.03, and the average loss per case was $208.44."

[46]"The approved Adjustment Bureaus are under intelligent, skillful, aggressive, well-trained and well supervised management. The honesty and integrity of every member of their personnel is beyond question. In order to secure the approval of the National Association of Credit Men, Adjustment Bureaus are required to comply with strict regulations covering organization, management, personnel, machinery, policies, protection of client's interests, care of correspondence, finances, records, and supervision by local boards of directors and by the National Association of Credit Men". *In Defense of the Nation's Receivables, supra* note 5, at 9.

present fee system for one of officialdom. Well paid governmental officers, receiving a regular salary bearing no relation to the business handled are suggested.[47] Competent and untemptable men would supposedly then be assured. But friendly adjustment, it should be remembered, also functions upon a fee basis. And because it is in the nature of a business, since it must have cases to be able to support its organization, it would seem open to the similar dangers of solicitation prevalent in the bankruptcy system.[48] In fact, investigation into the affairs of the bureaus in certain large cities (Chicago, Cleveland, Pittsburgh) discloses that during some period of their existence a change in personnel has resulted from conditions which have been interpreted to resemble partially the "ring" situation in bankruptcy.[49] Bureau officials are not magnanimously overpaid. They are but human beings, subject to the same temptations and weaknesses of others.[50] And, in the informality of the system, there is no intricate, elaborate procedure of checks and accountability such as the Bankruptcy Law provides. Nor is there any opportunity for public scrutiny. Bankruptcy defects in this regard, are unremedied in friendly adjustment which itself bristles with possibilities that are little short of startling. So much then for the question of repeated appointments, and the considerations of skillful merchandising, competent staffs, and "rings" to which it leads.

Considering now the actual mechanics by which the cash is realized, a major objection to the marketing system employed in bankruptcy is that it requires the use of the public auction sale, which, with its "resulting low returns", is forced upon the trustee. The low returns are caused by the expense of such a sale, and the inadequacy of the bids due to its "forced" character. Yet another objection is that the trustee's sale in bankruptcy is held only after such a period of time that the item "rent for administration expenses" consumes practically all of the proceeds derived from the sale, whereas the flexibility of the friendly adjustment system permits almost immediate reduction

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[47]See report, IN THE MATTER OF AN INQUIRY, ETC., *supra* note 7, at 43, also at 85, 88, where out-and-out official administration is considered. Partial officialdom is recommended. But see Coles, *op. cit. supra* note 37, at 435.

[48]"The Bankruptcy Committee of the American Bar Association in its 1924 report cited as a major evil the establishment of bureaus for liquidation work, the maintenance of which depends upon 'the earning of fees resulting from methods which are not only parallel with but encourage the practices of those attorneys whose activities are condemned'." Report, IN THE MATTER OF AN INQUIRY, ETC., *supra* note 7, at 177.

[49]See *infra* note 72.

[50]See *infra* note 108.

to cash. The problem can best be considered in two parts: (1) the time element involved, and (2) the prices obtained.

As to time, friendly adjustment undoubtedly has much the advantage. In this it presents its greatest appeal. Where no receiver is appointed, the sale cannot be held in bankruptcy until a trustee is elected or appointed. During the interval, rent mounts, insurance premiums accrue, watchmen's expenses may be necessary, and the goods may deteriorate, or the season for their best marketability may pass. Friendly adjustment, however, can theoretically reduce the assets to cash the day after it receives the case. The importance of this item cannot be over-estimated. However, where there is a receiver appointed in bankruptcy, the difference in powers would not seem great, for such receivership appointments are very often made upon the same day the petition is filed, or upon one immediately following.[51] A prompt receiver's sale, of course, reduces the above expense items.[52] And in districts like New York in which the prerequisite of "absolutely necessary" for the appointment of a receiver is so

[51]The following represents the lapse of time in days between the filing of the petition and the appointment of the receiver in 100 cases picked at random in The Yale New Jersey study:

Appointed	on same day:	67
"	" following day:	10
"	2 days:	5
"	3 days:	4
"	4 days:	2
"	5 days:	2
"	6 days:	1
"	8 days:	3
"	10 days:	1
"	20 days:	1
"	22 days:	1
"	40 days:	1
"	41 days:	1
"	74 days:	1

[52]"With a few exceptions, in the larger urban centers, and in many of the smaller ones throughout the country, the necessity of going forward promptly with administration in asset cases is recognized, and receiverships, as well as receivers sales, are common." Report, IN THE MATTER OF AN INQUIRY, ETC., *supra* note 7, at 106.

"...the average length of time elapsing between the sale and the petition in bankruptcy was approximately 34 days in the involuntary and 23 days in voluntary cases (for New York City). In Bankruptcy cases studied by Mr. Billig and Mr. Ritter in Pittsburgh, Cleveland, Detroit, and St. Paul, the average between the date of petition and sale was 51 days." *Ibid.* 196.

The results in the Yale New Jersey study indicate little activity upon the part of receivers, in spite of their prompt appointment, to capitalize upon their powers to effect quick sales. Out of 82 cases picked at random, the average between the petition and sale dates was 40.5 days.

liberally construed that a receiver is appointed at least in every asset case, the time consumed in reducing the assets to cash should be little more than in friendly adjustment, with the single reservation of the involuntary case in which the adjudication is contested and no consent to sell can be secured.[53]

It is to be noted also, for the purpose of speeding up the reduction to cash process, the use of the private sale is not outside the powers of bankruptcy.[54] It has been intimated that the private sale is only a "theoretical" possibility.[55] But investigation shows it to be a device that often is employed,[56] and the method is frequently used for the sole purpose of a quicker sale.

In the matter of advantageous prices there seems to be no inherent reason why receivers and trustees in bankruptcy cannot invoke the same means of producing buyers as can the bureau liquidator. Investigation discloses that this is the case.[57] Knowledge as to who are the persons and agencies interested in buying the various kinds of stocks is not limited to the friendly adjustment liquidator. The oft-appointed bankruptcy official also possesses such common, or easily acquired knowledge. The public auction method also has been charged to be a source of difficulty. But friendly adjustment itself is committed to the public auction method.[58] And the private sale is also used in bankruptcy.

[53]The statement has been made that "the very fact that creditors have six months from the date of the adjudication in which to file their claims [in bankruptcy] makes the period of liquidation normally a long one, and the item of administration rent is bound to be correspondingly high." Billig, *Extra-Judicial Administration of Insolvent Estates, supra* note 2, at 309. This, of course, is not true. The late filing of proofs of claim has no relation to a quick sale of assets for the purpose of leaving the place of business, thereby reducing the rent and other items involved.

Also, the Bulk Sales Acts of the various states, often calling for notices, extensions of time, etc., must frequently be considered in friendly adjustment. See example cited in Billig, *Extra-Judicial Administration of Insolvent Estates, supra* note 2, at 316.

[54]General Order XVIII authorizes the use of the private sale.

[55]Billig, *What Price Bankruptcy: A Plea for "Friendly Adjustment", supra* note 2, at 418.

[56]In the Yale study, out of 100 cases in which there were sales (picked at random from the New Jersey cases), private sales were effected in 34.

[57]In Chicago, the professional receivers keep files of all buyers they have done business with or know of, and also use the classified section of the telephone directory. To these are sent notices of the stock being offered. The sales department of the Irving Trust Co. is also a highly organized unit.

[58]Billig, *Extra-Judicial Administration of Insolvent Estates, supra* note 2, at 299.

So far as the "forced" character of the sale is concerned, both systems, it would seem, are on a par. Generally, all sales of insolvent estates are "forced". The goods must be disposed of. Buyers know this, and will not feel impelled to offer more for stocks of insolvent estates, whether sold through the bankruptcy or the friendly adjustment system. Furthermore, if the assets are to be sold immediately, as friendly adjustment prides itself in being able to accomplish,—and which would be necessary at any rate for a reduction of the rent item,—the sale would appear to be all the more "forced", since time cannot be consumed in a prolonged search for the highest bidder. In other words, the quicker the sale the more "forced" it might be.[59]

At this point in either system we encounter the second type of "ring" above referred to, that is, the auctioneer and his co-workers who conspire to force the sale of such insolvent estate stocks at unfair and practically "fixed" prices. This phase of the "ring" problem is not a matter of systems. Prospective bidders at the friendly adjustment sale may collude to stifle bids, and obviously little can be done about it. Friendly adjustment, however, is described as employing the following method of insuring an "honest auction". "[T]he bureau auctioneer is instructed first to take bulk bids on certain lots of stock, and later to take piecemeal bids on the same lots from various buyers. If the bulk bid for a certain group of items totals more than the piecemeal bids for the same group, the bulk bid will prevail, and *vice versa.*"[60] But this identical type of public auction is commonly held under the Bankruptcy Act,[61] concerning which charges of fraud and dishonesty have been made. This method of sale will not prohibit a "ring" from its activities. It can control both piece-lot and bulk bids. Auctioneers have been charged to "knock-down" piece-lot bids at low figures, so that the later bulk bid will far exceed the piece-lot bids (or *vice versa*) and by comparison seem a fair and honest offer, whereas in reality it is also a low, controlled price. In

From a study made by the U. S. Department of Commerce of 25 cases closed in friendly adjustment by the Newark, N. J. Bureau, representing the bulk of such work done by the Bureau in the past two years, those cases in which records of sales could be secured showed 7 private sales and 4 by public auction.

[59]Bonbright and Pickett, *op. cit. supra* note 14, at 598.

[60]Billig, *Extra-Judicial Administration of Insolvent Estates, supra* note, 2, at 311.

[61]Out of 80 public auction cases in the Yale New Jersey study, picked at random, this method was employed in 72.

The method is commonly required by district rules. See Bankruptcy Rule 8, E. Dist. of N. Y.; Bankruptcy Rule 8, So. Dist. N. Y. New Jersey has no such rule.

bankruptcy, at least, there is the further check of the appraisal of the bankrupt's estate by the three appraisers required by Section 70b of the Act.[62]

Still another feature in which friendly adjustment claims to excel bankruptcy in the realization of assets is in the manner of the collection of outstanding accounts receivable. Any success whatsoever in this regard is sufficient to warrant a claim of superiority.[63] While the claim seems to fail of substantial proof,[64] it would appear that a system giving over a part of its organization to the handling of such accounts, as does friendly adjustment, should undoubtedly give more

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[62]Of course a capable "ring" would also control the appraisers.

[63]The following is a tabulation of the results of collection of accounts receivable in 100 cases picked at random in the New Jersey study:

	Amt.Sched.	*Amt.Realized*		*Amt.Sched.*	*Amt.Realized*		*Amt.Sched.*	*Amt.Realized*
1.	13.50	0	35.	2000.00	0	69.	3264.06	0
2.	373.99	0	36.	1346.94	306.24	70.	25.00	0
3.	2200.00	0	37.	121.00	0	71.	233.30	100.86
4.	7720.21	3.58	38.	143.63	0	72.	229.97	0
5.	12655.13	0	39.	53.45	0	73.	4001.98	0
6.	1675.52	0	40.	40.00	0	74.	166.66	0
7.	7500.00	0	41.	707.09	90.46	75.	15.75	0
8.	138.38	0	42.	5939.78	3000.00	76.	18.69	0
9.	2367.43	1832.97	43.	71.93	0	77.	600.00	0
10.	62.47	15.46	44.	1110.50	0	78.	4059.40	0
11.	246.00	0	45.	1945.00	100.00	79.	40.00	0
12.	2573.80	0	46.	12975.01	0	80.	13534.93	0
13.	292.60	0	47.	217.37	0	81.	200.00	0
14.	1000.00	334.87	48.	113.70	0	82.	7.50	0
15.	2516.30	20.00	49.	2247.63	186.67	83.	215.37	0
16.	2632.50	0	50.	51317.66	0	84.	8771.12	0
17.	135.45	8.00	51.	400.00	0	85.	18.25	0
18.	18300.03	15026.45	52.	3420.00	0	86.	241.05	0
19.	1400.00	11.25	53.	221.00	15.00	87.	32.90	0
20.	122.90	0	54.	6125.45	3715.94	88.	1382.61	51.32
21.	164.75	0	55.	49.20	0	89.	1298.00	0
22.	140.63	25.00	56.	88.00	0	90.	3344.00	0
23.	40.00	0	57.	658.06	604.70	91.	104.95	15.00
24.	10.00	0	58.	1122.79	0	92.	2168.50	0
25.	543.68	0	59.	151.14	24.89	93.	684.00	0
26.	4133.84	118.85	60.	5000.00	14.87	94.	795.91	0
27.	1285.99	5.00	61.	2260.00	0	95.	949.49	0
28.	2378.19	0	62.	88.40	0	96.	300.00	0
29.	700.00	0	63.	150.00	0	97.	2903.49	337.49
30.	14346.81	303.60	64.	3.00	0	98.	2700.00	0
31.	6447.76	79.08	65.	1400.00	60.20	99.	510.52	0
32.	0	11.00	66.	1963.80	2226.84	100.	909.40	415.00
33.	223.67	0	67.	86.95	0			
34.	10409.00	0	68.	165.00	0			

[64]See Billig, *Extra-Judicial Administration of Insolvent Estates, supra* note 2, at 299, n. 14, in which but three cases are cited as follows: 1. of $16,432.18, $15,902.48 was collected; 2. of $22,842.85, $16,661.44 was collected; 3. of $36,041.02, $26,298.06 was collected. Similar cases showing success in this matter may also be selected from the bankruptcy court records.

satisfactory results. Yet on the other hand organized collection agencies such as those of friendly adjustment not only may be, but actually are set up under the Bankruptcy Act.[65] It should also be remembered that, in bankruptcy, invariably either the lawyer-receiver, or the lawyer-trustee, or the receiver's or trustee's attorney will handle such collections. When the average business man wishes to place the collection of an account into reliable hands, the matter is very often entrusted to an attorney. Bankruptcy, in effect, *ipso facto* does this for the creditor.

Collecting the accounts receivable of any insolvent or financially embarrassed estate has baffled the best minds, whatever the method. When a business is being liquidated, whether it be by means of equity receivership, bankruptcy, official bureau of friendly adjustments, or un-official creditor trust-deed arrangements, the psychology of the one indebted to the insolvent's estate is the same. It is a well known psychology that reduces such accounts to practical worthlessness. It is comparable to the "forced" character of the sale of the insolvent's goods. Again, by the time the estate finds its way into the liquidating system's hands, be it bankruptcy or friendly adjustment, the debts

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The following are the available results from the 25 Newark cases studied in friendly adjustment:

	Appraised	*Collected*
1	———	———
2.	———	———
3.	$ 75.00	$ 24.00
4.	300.00	no record of
5.	10.94	10.94
6.	14.00	no record of
7.	57.05	no record of
8.	1600.00	1400.00, lump sum which includes stock appraised at $1000.00
9.	———	———
10.	400.00	300.00, lump sum which includes stock appraised at $650.00
11.	400.00	no record of
12.	125.00	no record of
13.	337.00	no record of
14.	1000.00	100.00
15.	———	———
16.	2573.80	none
17.	94.00	25.71
18.	———	———
19.	———	———
20.	100.00	100.00
21.	———	———
22.	3152.62	no record of
23.	———	———
24.	———	———
25.	———	———

[65]The Irving Trust Co. is an example.

are often old ones, which the insolvent himself has already long tried to collect. Their uncollectibility is often a primary cause of the failure. Rarely does a going concern collapse suddenly. Its death is invariably preceded by a long, drawn-out illness, a period during which all available resources have been continuously summoned to stave off the impending disaster. So that the *cause* of the accounts being uncollectible is essentially not the fact that the estate is being liquidated by a poor system, but rather is to be found buried in events of months long standing. In other words, the debt comes to bankruptcy—or friendly adjustment—a bad one. Debtors move. They have unknown addresses. They become financially irresponsible and judgment proof. They disclaim liability. It seems impossible that friendly adjustment can often change the actual course of human events. If anything, bankruptcy, as a system, would seem to be in an advantageous position because of the powers granted under 21A of the Act which would allow the subpoenaing of debtors.

In one important phase of the collection problem is the friendly adjustment system inherently at a distinct advantage, however. Bankruptcy liquidation is effected publicly. Much of the debtor's psychology above referred to would not be a troublesome factor if he did not know of his creditor's financial embarrassment. But friendly adjustment works quietly. It is not an official system and need have no publicity. If the business remains open under a receiver in bankruptcy, however, this difficulty is partially over-come.[60] No remedy for this phase of the problem, of course, is possible. In fact, if the friendly adjustment system were given legal recognition, as has been advocated, its advantage in this particular would be dispelled.

II. Creditor Non-Cooperation

The observance has often been made that creditors do not cooperate in the ordinary bankruptcy case, and, of course, this is too com-

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[60]Billig, *What Price Bankruptcy: A Plea for "Friendly Adjustment"*, *supra* note 2, at 419.

This fact is commonly recognized, and a frequent New Jersey allegation for the appointment of a receiver is "Petitioner further shows that he has information that the bankrupt has outstanding accounts which demand attention; that if the debtors become advised of the bankruptcy herein they will delay making payments through various pretexts and excuses, and some will move and the accounts become lost..."

See Case No. 18, *supra* note 62, in which this was the situation.

monly known to dispute.[67] Claims are assigned. Little regard is

[67]The following represents results, in 75 asset cases picked at random in the Yale New Jersey study, of creditors recorded as attending in person the meetings and hearings designated below.

	Creditor's Meetings		*Sales Hearings*		*21A Exams.*	
	Sched. Cred.	*No. Held*	*Total Attending*	*No. Held*	*Total Attending*	*No. Held*	*Total Attending*
1.	16	3	0	2	0	1	1
2.	20	2	0	0	—	0	—
3.	28	4	0	3	1	0	—
4.	93	3	0	2	1	4	0
5.	12	7	0	0	—	5	0
6.	88	7	1	3	0	4	0
7.	19	2	0	2	0	1	0
8.	50	3	0	2	0	1	0
9.	40	2	0	2	0	0	—
10.	20	2	0	2	0	1	0
11.	35	4	0	2	0	2	0
12.	24	3	1	2	0	11	0
13.	108	2	0	2	0	0	—
14.	26	2	2	1	1	0	—
15.	75	2	0	1	2	2	0
16.	15	2	0	2	0	1	0
17.	14	2	0	1	0	1	0
18.	5	3	0	4	0	4	0
19.	106	2	0	0	—	2	0
20.	15	2	0	1	0	0	—
21.	20	3	0	2	0	0	—
22.	19	2	0	1	0	1	0
23.	29	2	0	2	0	1	0
24.	78	5	3	2	0	2	0
25.	24	3	0	3	0	0	—
26.	48	2	0	0	—	0	—
27.	22	2	0	2	0	1	0
28.	20	3	0	2	0	1	0
29.	10	3	0	0	—	0	—
30.	30	2	0	1	0	0	—
31.	23	2	0	0	—	0	—
32.	16	2	0	1	0	0	—
33.	32	2	0	2	0	1	0
34.	63	2	1	0	—	0	—
35.	50	2	1	0	—	0	—
36.	78	2	0	1	0	1	0
37.	55	3	0	2	0	0	—
38.	16	2	0	2	2	1	0
39.	14	2	0	2	0	0	—
40.	96	2	0	0	—	0	—
41.	87	3	0	2	0	1	0
42.	38	2	0	2	0	1	0
43.	21	2	0	0	—	0	—
44.	9	4	0	3	0	1	0
45.	29	3	0	2	1	1	0
46.	28	2	1	0	—	0	—
47.	9	2	1	0	—	0	—
48.	51	3	0	0	—	0	—
49.	2	3	0	0	—	0	—
50.	25	2	1	1	0	0	—
51.	28	3	0	2	0	0	—

given to the election of a trustee.[68] The entire matter of lack of creditor interest is declared to be a wide open door for the entry of fraud. The breakdown of the theory of creditor control upon which the Bankruptcy Act is based has conclusively been proved.[69]

Friendly adjustment, however, claims that it succeeds in obtaining and therefore enjoys the benefits of creditor control, which is its

	Creditor's Meetings			*Sales Hearings*		*21A Exams.*	
	Sched. Cred.	*No. Held*	*Total Attending*	*No. Held*	*Total Attending*	*No. Held*	*Total Attending*
52.	12	3	0	0	—	0	—
53.	40	1	(comp. case) 0	0	—	0	—
54.	38	5	0	0	—	4	0
55.	15	3	0	0	—	0	—
56.	49	3	1	3	0	0	—
57.	6	2	0	0	—	0	—
58.	49	2	3	0	—	0	—
59.	8	2	0	0	—	0	—
60.	31	5	2	0	—	0	—
61.	37	2	0	2	1	1	2
62.	35	2	2	2	0	0	—
63.	36	2	0	2	0	0	—
64.	21	3	2	0	—	0	—
65.	138	2	0	5	0	1	0
66.	18	4	0	2	0	1	0
67.	334	2	0	2	0	6	0
68.	73	3	0	3	0	1	0
69.	32	2	0	2	0	1	0
70.	111	2	0	2	0	1	0
71.	11	2	0	2	0	1	0
72.	41	2	0	4	0	1	0
73.	64	2	0	2	0	1	0
74.	46	2	0	2	1	1	0
75.	47	2	0	0	—	0	—

[68]The recent Supreme Court promulgation, (Jan. 13, 1930) amending General Order 39 which prohibits the soliciting of claims should be noted in this connection:

"The local Bankruptcy Court, may, however, when a banking institution is under local rule or practice always appoint a receiver in cases requiring the services of a receiver, by local rule approved by a majority of the Circuit Judges of the Circuit, provided that notice may be given to the creditors of the availability of such institutions as trustees if elected, and may provide means to facilitate the creditors in filing and voting their claims in favor of such institution as trustee."

In New York City, the referee to whom the case is assigned sends to all creditors a prepared proof of claim with proxy clause authorizing the referee to vote the claim of the creditor in favor of the Irving Trust Co. as trustee.

In the Yale New Jersey study, out of 100 cases selected at random, in 91 cases, the trustee was appointed by the referee, in 3 he was elected by creditors, and in 6, he was appointed by the referee at the suggestion of creditors.

[69]See report, IN THE MATTER OF AN INQUIRY, ETC., *supra* note 7, at 23, 128, 137. Also, *infra* note 76.

underlying philosophy.[70] But claims of remarkable success achieved on this score in friendly adjustment must be taken guardedly. The phrase "creditor participation" as applied to friendly adjustment would seem to imply many meetings, active attendance and much time spent upon deliberating the methods of best liquidating the estate. Evidence of success in this respect in some of the bureaus does not seem to be forthcoming.[71] In other bureaus,[72] more than often, however, it has been found that "creditor participation" proves to be nothing more than a matter of the bureau liquidator keeping in telephone touch with certain of the available creditors, or mailing notices advising of major moves in the settlement of the estate.[73] These notices

[70]See *supra* note 3.

[71]Testimony of Mr. Sheckell of the New York Credit Men's Association. Report, IN THE MATTER OF AN INQUIRY, ETC., *supra* note 7, at 220:

"...The business man has been charged with not taking an interest in Bankruptcy proceedings. I want to state that in Friendly Adjustment of the same type cases, the business man takes a very keen interest in 95 or 97% of the cases handled by our offices under the Friendly Adjustment plan. Under this plan we have a creditors' committee..."

The following results were computed from the government study of Friendly Adjustment cases in Newark, N. J., where such information was available. All data was offered to the government by the Bureau from its files.

Case No.	*No. of unsecured creditors listed in the debtor's statement of liabilities*	*Creditors attending each meeting*	*No. of Meetings*
1.	46	20	4
2.	19	15	1
3.	28	20	3
4	5	5	2
5.	77	55	2
6.	23	18	1
7.	19	12	4
8.	14	6	1
9.	87	40	3
10.	20	10	1
11.	115	60	4
12.	21	10	2
13.	24	10	1
14.	13	5	1
15.	10	4	1
16.	29	15	1
17.	54	35	2
18.	56	40	5
19.	17	7	1

Average results: 57.16% of the creditors attended; 2.1 meetings held per case.

[72]By Mr. Paul O. Ritter as a result of his visits to several bureaus, as a member of the staff for the committee submitting the report.

[73]See report, IN THE MATTER OF AN INQUIRY, ETC., *supra* note 7, at 220, where the co-operation of creditors obtained by the Irving Trust Co. and in friendly adjustment is termed "merely advisory and informal".

indeed seem to be a *forte* of the friendly adjustment system.[74] But identical notices are a mandatory requisite in bankruptcy.[75]

Lack of creditor participation and interest is expected as a general defect in the liquidation of any insolvent's estate. Business men do not wish to waste any more time or money on an already unprofitable investment. No insolvency participation is a profitable enterprise to the business man who is engaged in present, pressing, money-making ventures.[76] Consequently, the assignment of claims and subsequent refusal to participate any further in the proceedings, which is complained of in bankruptcy, is largely duplicated in friendly adjustment.[77]

Some of the lack of direct creditor interest exhibited in bankruptcy might possibly be explained also by the fact that the bankruptcy system provides the creditors with a receiver, trustee, and their attorneys, who are direct legal representatives of the creditor's interests. To procure such representation in friendly adjustment, the creditor

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[74]Billig, *What Price Bankruptcy: A Plea for "Friendly Adjustment", supra* note 2, at 430.

[75]Section 58 of the Bankruptcy Act, provides for 10 days notice by mail to creditors of all examinations, hearings upon application for confirmation of compositions, meetings, sales hearings, dividend payments, trustee's final accounts filings, compromises, dismissal of proceedings and 30 days' notice for applications for discharges. These notices may also be published in newspapers, that of the first creditors' meeting being so required.

"Adjustment bureau practice strictly insists that each creditor have an opportunity to be heard". Billig, *What Price Bankruptcy: A Plea for Friendly Adjustment", supra* note 2, at 430. The above notices would show the same to be true in bankruptcy. Creditors being advised, however, does not mean "creditor participation" exists.

It should be noted that the committee submitting the report, IN THE MATTER OF AN INQUIRY, ETC., *supra* note 7, at 54 recommends the future omission of many of these requisite notices as a means of speeding up the liquidation of the estate.

[76]Testimony of Hon. Paul Jones, District Judge, No. Dist. Ohio, in the report, IN THE MATTER OF AN INQUIRY, ETC., *supra* note 7, at 142: "The lack of interest of creditors and their failure generally to participate in bankruptcy proceedings is to be expected, and I do not know of any way to stimulate their interest".

Testimony of Hon. Albert H. Reeves, District Judge, W. D. Mo.: "I do not believe that creditors can be incited to take greater interest than at present. The reason is that the bankrupt is hoplessly insolvent when he resorts to Bankruptcy". *Ibid.*

Testimony of Hon. J. Foster Symes, District Judge, Dist. Colo.: "Creditors will not, and cannot, be made to show sufficient interest." *Ibid.*

[77]See *supra* note 72.

would have to employ his own attorney and himself assume the payment of the fee from which the bankruptcy system relieves him. Personal attendance by local creditors, if there be any, may probably be explained by this circumstance, or else by the novelty of this different type of liquidation proceeding. In most cases, however, the absentee creditors far outnumber local creditors.[78] That the former

[78]This is taken cognizance of in the report, IN THE MATTER OF AN INQUIRY, ETC., *supra* note 7, at 10.

The following represents the number of local and absentee creditors in 100 cases picked at random in the Yale New Jersey study:

	"Locals"	*"Absentees"*		*"Locals"*	*"Absentees"*
1.	0	16	45.	13	15
2.	0	20	46.	0	9
3.	9	19	47.	9	42
4.	47	46	48.	0	2
5.	1	11	49.	8	16
6.	3	85	50.	0	28
7.	11	8	51.	1	11
8.	11	41	52.	3	37
9.	32	8	53.	0	24
10.	6	14	54.	0	15
11.	3	17	55.	0	79
12.	9	15	56.	6	110
13.	7	102	57.	0	49
14	9	17	58.	1	43
15.	9	69	59.	0	8
16.	3	12	60.	37	104
17.	13	1	61.	10	38
18.	3	2	62.	8	29
19.	3	97	63.	12	23
20.	0	15	64.	0	6
21.	2	18	65.	4	32
22.	15	3	66.	10	11
23.	0	29	67.	0	52
24.	3	75	68.	15	25
25.	17	7	69.	0	148
26.	1	47	70.	8	127
27.	3	19	71.	3	15
28.	17	3	72.	28	54
29.	1	9	73.	8	25
30.	6	23	74.	21	313
31.	1	22	75.	1	25
32.	2	39	76.	0	73
33.	7	9	77.	16	16
34.	41	20	78.	0	111
35	13	37	79.	8	3
36.	1	77	80.	0	81
37.	6	49	81.	6	35
38.	0	16	82.	0	23
39.	8	6	83.	0	11
40.	0	96	84.	1	63
41.	5	82	85.	5	41
42.	1	37	86.	6	12
43.	10	11	87.	0	12
44.	8	1	88.	4	18

should come in from other cities to pass judgment upon details of the administration is obviously not to be expected.[79] Thus, the necessity of their leaving such details to others is the same in friendly adjustment as in bankruptcy. Their "cooperation" would probably mean much more time and money lost than would be returned to them as a result of it. Since the great majority of the claims are comparatively small, a dividend of $20.00 in friendly adjustment rather than one of $10.00 in bankruptcy on an average $100.00 claim would hardly seem to be sufficient inducement. From the business man's point of view, the details of the liquidation should be handled by others appointed for the purpose, whoever the liquidator be.

The suggestions of Mr. Billig in this regard would seem, therefore, not to be of great importance. They are: (1) "Provide in the Act for the official recognition by the bankruptcy court of the recommendations made by a bona fide creditors' committee, especially with respect to the appointment of the receiver..." (2) "The exercise of such powers [broad powers to be given receivers and trustees], however, should be conditioned on the approval in writing of the creditors' committee..."[80] But in England, where similar features are a part of the Bankruptcy Act, they rarely play a role, having no importance or significance in the vast majority of cases.[81]

	"Locals"	*"Absentees"*		*"Locals"*	*"Absentees"*
89.	0	47	95.	12	22
90.	5	62	96.	0	8
91.	0	43	97.	0	18
92.	0	38	98.	7	42
93.	0	174	99.	4	2
94.	0	15	100.	5	53

Average "locals" per case: 7.64. Average "absentees" per case: 39.27. Percentage "locals" to "absentees": 19.46%.

[79]Either the results in the Newark Bureau cases, *supra* note 71, show that the Bureau there is accomplishing this remarkable feat, or else the cases themselves are unusual in the numbr of local creditors they involve; or possibly closely adjoining New York City should be regarded as "local" for purposes of creditor location.

[80]Billig, *Extra-Judicial Administration of Insolvent Estates, supra* note 2, at 319.

[81]See article appended to report, IN THE MATTER OF AN INQUIRY. ETC., *supra* note 7, at 279, giving a detailed picture of the workings of the English Act. For "small bankruptcies" there is a summary administration. *"Orders for summary administration are made in 80% of the cases.* (Italics the writer's). Thus in the great bulk of cases there is single administration by official liquidating organizations. There is no Committee of Inspection (creditors). Experience having shown that creditors take little or no interest in these small bankruptcies, the machinery for creditor control is made negligible. A non-official trustee can be put in control only by a special resolution (¾ in amount, majority in number of creditors present or represented at the meeting)."

III. High Cost of Administration and Low Returns to Creditors—Statistics

The bankruptcy reports of the Attorney General have been invoked to illustrate the low percentages realized by general creditors on their unsecured liabilities. For a representative year, the returns were shown to be as low as 10.11% for involuntary cases and 6.48% for voluntary cases.[82] No attempt to dispute the generally accepted assumption of meager dividend returns derived from bankruptcy proceedings is here contemplated. Nevertheless, the results based on the Attorney General's figures should not be taken at their face value in proving this assumption. The results reached are too low. This is so because analysis discloses the basic figure "total liabilities" in the Attorney General's reports is, firstly, exaggerated, and secondly, even

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Ibid. 308: "The experience of the English points to the conclusion that it is impossible to secure keen creditor interest in the average case. The trading class in England are literate and informed as to the condition of estates in which they are interested. Their committees of inspection are invested with broad powers of control and supervision. *Yet active creditor control is not achieved.* (Italics the writer's). The trustee administers as he sees fit, subject only to the audit of his accounts by the Board of Trade."

But because there may be cases in which creditors might, for some reason or other, decide to step in, it would seem of no harm to have such provisions. Other acts containing similar provisions are:

England: 46 and 47 Vict. c. 52 (1883) as amended by 16 and 17 Geo. V, c. 7, §§20, 56-58, 79 (1927).

Canada: 9 and 10 Geo. V, c. 36 (1919) as amended by 10 and 11, Geo. V, c. 34 (1920) and 11 and 12 Geo. V, c. 17, §§20, 21, 43 (1921).

Germany: Konkursordnung (Commercial Laws of the World, vol. 21) §§84, 87-92, 129-234, 137, 149, 150, 159.

France has no such provisions in its Act.

The report itself is seemingly inconsistent with the article, however. At 27 and 28, recommendations are made for creditors' committees (inspectors), written consents, etc., similar to those made by Mr. Billig, with the observation that creditor participation would probably thus be secured *in the same manner in which it is secured in England,* among others (Canada, Friendly Adjustment, the Irving Trust Co. in New York). And at 221, "It seems reasonable to hope that by simplifying and speeding up the administration along suggested lines, by calling creditors together more promptly, and by giving creditors' committees a recognized status and official duties, the part of creditors in administration would become general instead of sporadic and isolated."

Of the 21 Newark cases closed in the Bureau by Friendly Adjustment, creditors' committes were appointed in only 8, there being no such committees in the other 13.

[82]Billig, *What Price Bankruptcy: A Plea for "Friendly Adjustment", supra* note 2, at 417, deducing from figures of the Rep. Atty. Gen. 1927 at 178.

if corrected, a false one upon which to base a comparison of the dividends resulting from the two systems.

Firstly, some of the many ways in which the figure is erroneous and bloated are:

1. Cases in which a partner individually goes bankrupt, but the remaining partners do not, the bankrupt partner, nevertheless, listing the partnership liabilities as his own. Partnership creditors, however, may derive satisfaction from the other partners.
2. Cases in which husband and wife go through bankruptcy proceedings separately, both listing themselves liable for identical debts.
3. The similar situation in which bankrupt corporations list the same debts for which the corporation officials also list themselves liable in separate bankruptcy proceedings.
4. Cases in which the same bankrupt duplicates a debt, on different pages of the schedules, all to be included into the bankrupt's final "total liabilities" figure. This occurs if the bankrupt or his attorney, feels uncertain as to the exact classification of a debt for the schedule sheet, and consequently, lists the debt on two pages, *i.e.*, listing the bankrupt's liability as endorser both on schedule A3 (Debts to unsecured creditors) and A5 (Debts which other parties ought to pay).
5. Cases in which debts are listed which have already received complete or partial satisfaction, or which will be fully or partially satisfied by guarantors and sureties.
6. Cases in which false or mistaken liabilities are listed, *i.e.*, debts which are in fact not enforceable obligations.[83]

These are but some of the more obvious ways in which the "total liabilities" figure, representing the amount of debts annually thrown into bankruptcy proceedings, is enlarged. It should be pointed out in what manner some of these errors are included. The duplications are obvious. As to the others, it is principally because the Attorney General's figures "total liabilities" is based upon the schedules as filed by the bankrupt. Included in the referee's final report of every bankruptcy case referred to him is the item "scheduled liabilities which have not been proved". These liabilities often make up a large part of the figure "total liabilities" of the individual cases, from which the Attorney General's final reports are derived, and it is this inclusion of unproved debts which the bankrupt nevertheless schedules—debts which may have never existed—which is the largest factor in the errors. Hence the official bankruptcy figures in this respect

[83]These typical duplications and errors glaringly appeared in an examination of over 1,000 schedules filed in New Jersey.

represent largely the bankrupt's own idea of his liabilities, fancied or actual, true or mistaken. It seems clear that these are errors and duplications which should be subtracted from the total amount of the stated Attorney General's figure.

In respect to other items affecting the net figures, in 1924, a corrected Attorney General's figure for the Southern District of New York for administration expenses, "corrected", not in the light of the above, but merely in eliminating office errors, showed a cost for this of about 15% of the net amount realized.[84] Figures quoted by Mr. Billig from an Attorney General's report of the fiscal year 1926-1927 and upon which he bases his comparison showed this expense to be about 24%, as compared with computed friendly adjustment costs of about 14%.[85] Likewise, the comparative returns to creditors have been concluded to be about 6% for the bankruptcy case, as against about 27½% for friendly adjustment. These figures in each case should receive an adjustment resulting from computations as to what is the true amount of "total liabilities" thrown into bankruptcy in which case the disparities are greatly reduced. Further, because it comes to the liquidator through sources other than the bankrupt, the friendly adjustment case more closely resembles involuntary bankruptcy which admittedly furnishes higher returns than in the voluntary. It should also be borne in mind that the erroneous duplications in bankruptcy liabilities are not counteracted by similar erroneous duplications or inflations of scheduled assets. The alleged dividend percentages are based upon actual "net assets realized", which figure is that of amounts actually derived by sale of assets, or otherwise. It bears no relation to the bankrupt's hopefully exaggerated idea of their value.

Secondly, for purposes of comparison especially, the Attorney General's "total liabilities" figure is a misleading one. This is so principally because of the inclusion of the no-asset case. These are cases with which the bankruptcy machinery must deal. Friendly adjustment on the contrary handles only cases which will at least support a fee for the bureau that will be compensatory. This business requirement would eliminate not only the strict no-asset case, but

[84]The figures were corrected at the request of the Merchants' Ass'n of New York. See report, MERCHANTS' ASS'N OF NEW YORK, *supra* note 10, at 13.

As a matter of fact, the figure "total liabilities" was increased, as was also, however, the dividend payments to creditors. They evidently had nothing to do with the type of "corrections" referred to in the article.

[85]Billig, *What Price Bankruptcy: A Plea for "Friendly Adjustment"*, *supra* note 2, at 436.

also hundreds of small asset cases not able to furnish such a fee. In other words, bankruptcy must accept any and all cases. Friendly adjustment can pick its cases. It itself examines and investigates the cases before it finally decides to accept.[86] Investigation discloses that the number of cases which friendly adjustment would not touch and with which the bankruptcy liability figure is burdened are many. Liabilities represented by no-asset cases with which the bureau could not bother and which for fair comparison would have to be deducted from the Attorney General's total liabilities figure, is enormous.[87] No attempt is made to gather even an approximate figure for the very small asset case with which also the bureau would not deal.[88] But this type of case shows necessity of further adjustment before fair statistical comparisons be attempted.

Moreover the publisbed charts illustrating the high dividend returns given to creditors in the "assignment" (liquidation, and therefore comparable to bankruptcy) cases do not include those cases begun in the Bureau as "extension" (continuation of the business) cases, and subsequently liquidated because of unsuccessful results. Much has been said of the splendid work done by the bureaus in thus *saving* financially tottering concerns, instead of merely liquidating the remains of tbe wreck.[89] Over-optimism about the results should again

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[86]*Ibid.* 429, 430.

The following figures represent the appraised assets in the 25 Newark friendly adjustment cases studied:

1.	$5340.00	14.	20280.00
2.	1220.00	15.	1583.50
3.	not apraised—524.00 realized	16.	not appraised—1470.20 realized
4.	1220.00	17.	not appraised—1584.42 realized
5.	510.94	18.	500.00
6.	814.00	19.	400.00
7.	63400.00	20.	100.00
8.	1721.00	21.	no record of
9.	600.00	22.	91635.00
10.	1850.00	23.	6700.00
11.	1000.00	24.	1500.00
12.	1500.00	25.	300.00
13.	1200.00		Average=$8,623.04

[87]In this country, nearly two-thirds of the cases are no-asset cases." Report, IN THE MATTER OF AN INQUIRY, ETC., *supra* note 7, at 35.

[88]"If we are to add to the no-asset cases those in which the assets are only a hundred dollars or so, the proportion of cases in which no dividends, or nominal dividends are paid, would be far higher than two-thirds." *Ibid.*

"The great majority of cases, placed as high as 75%, are comparatively small bankruptcies". *In Defense of the Nation's Receivables, supra* note 5, at 9.

[89]Billig, *Extra-Judicial Administration of Insolvent Estates, supra,* note 2, at 300; Billig, *What Price Bankruptcy: A Plea for "Friendly Adjustment", supra* note 2, at 428; *In Defense of the Nation's Receivables, supra* note 5, at 9.

be cautioned against. Recent research in the equity receivership, a system designed to continue the business, inject new life, by reorganization if necessary, in short, to *save* rather than liquidate, illustrates how lean have been such results.[90] To make the figures fairer, then, the outcomes of these unsuccessful "extension" cases should be added to the liquidation tables. Inferentially from the results in equity receivership there are many nonsuccesses. On the other hand cases begun in equity receivership that subsequently found their way into the bankruptcy court should also be deducted from the bankruptcy figures.

As the whole matter of proof by statistical data is often dismissed with the cynical "axiom" that "anything can be proved by statistics" this interesting subject will be dismissed with the admission that regardless of specific figures, Mr. Billig's excellent charts camparing the results of liquidation by means of the two systems, of similar type businesses seem, on the whole, to show returns in favor of friendly adjustment.

This adverse showing of the bankruptcy system is due primarily, of course, to the general high cost of administration that this system seems to require, and which consumes practically everything that is realized from the estate. In general, this fact must be admitted.[91] It

[90]See Douglas and Weir, *Equity Receiverships In The United States District Court For Connecticut*, 4 CONN. B. J. 1.

3 of the 25 Newark Friendly Adjustment cases have already gone to court. 8 more were extension cases that were still open.

[91]The following represents results of 100 asset cases picked at random in the Yale New Jersey study.

	Net Amount Realized	*Cost of Adm.*		*Realized Net Amount*	*Adm. Cost of*
1.	$ 464.46	$ 464.46	20.	1586.28	1329.76
2.	6427.28	2271.33	21.	992.64	533.54
3.	7378.82	2022.22	22.	5233.28	2939.10
4.	2630.00	736.99	23.	2103.42	2103.42
5.	3957.09	2270.48	24.	1866.23	806.46
6.	262.00	262.00	25.	4349.96	944.16
7.	12106.89	4716.22	26.	12007.19	4595.12
8.	290.94	290.94	27.	1929.93	1110.78
9.	3903.85	2201.47	28.	1508.42	930.91
10.	6362.87	3126.24	29.	2672.83	2207.63
11.	135.22	135.22	30.	26703.20	2603.62
12.	258.61	258.61	31.	1253.50	653.50
13.	8678.95	4795.51	32.	985.00	636.95
14.	11708.02	4478.14	33.	2282.57	681.04
15.	2760.51	1862.31	34.	600.00	505.43
16.	3480.54	2244.78	35.	13297.35	3422.17
17.	11102.98	3102.98	36.	1694.37	928.41
18.	116.04	116.04	37.	653.80	603.80
19.	415.90	415.90	38.	41.45	41.45

has its effect particularly upon the small cases, in which the net amount realized from the assets seldom exceeds the costs of administration. But several matters must be kept in mind before we come to a too condemnatory conclusion. Admitting that bankruptcy is more expensive than friendly adjustment, as seems to be the general situation when any extra-legal settlement is compared with a court machinery process, it is submitted that bankruptcy gives much more for its

	Net Amount Realized	*Cost of Adm.*		*Net Amount Realized*	*Cost of Adm.*
39.	557.42	443.21	70.	211.00	198.83
40.	985.02	758.19	71.	117.94	117.94
41.	455.81	416.89	72.	773.06	501.93
42.	17620.04	7272.14	73.	333.54	183.06
43.	1443.74	1060.62	74.	885.63	420.01
44.	1125.60	858.21	75.	714.31	646.02
45.	500.00	500.00	76.	2876.65	1296.91
46.	406.71	406.71	77.	5350.00	2643.10
47.	550.00	483.36	78.	690.70	358.18
48.	535.00	231.59	79.	445.65	424.16
49.	525.00	465.29	80.	330.15	149.95
50.	2825.20	1646.86	81.	89.10	89.10
51.	9069.43	3143.27	82.	795.75	795.75
52.	445.65	424.16	83.	345.00	265.85
53.	660.00	412.86	84.	2652.31	543.39
54.	8976.85	3099.43	85.	5570.52	1097.48
55.	609.67	585.01	86.	454.25	369.59
56.	92.42	91.32	87.	3062.20	1490.55
57.	258.55	258.55	88.	1030.50	830.50
58.	1030.80	908.80	89.	1194.94	677.75
59.	59.08	59.08	90.	1592.57	1305.78
60.	1096.38	215.08	91.	1581.39	830.08
61.	400.00	400.00	92.	1505.94	1505.94
62.	60.56	60.56	93.	353.00	353.00
63.	991.70	991.70	94.	5685.70	385.30
64.	92.05	92.05	95.	240.00	123.97
65.	12035.07	2806.77	96.	2114.35	820.42
66.	424.71	64.71	97.	627.77	410.45
67.	6671.76	2381.82	98.	334.38	178.13
68.	1503.89	1304.50	99.	2622.67	1522.65
69.	165.84	79.79	100.	7347.38	3035.42
Total	273,090.77	118,643.03		Percentage consumed=43.444%.	

The following dividends were paid in the Newark Bureau cases:

1. 85.5%
2. 20%
3. court case
4. none
5. 6½%
6. 47.8%
7. still open
8. court case
9. 37%
10. none
11. still open
12. 20%
13. 13¼%
14. 76.7 %
15. 35%
16. court case
17. court case
18. still open
19. 19%
20. none
21. 14%
22. still open—10% thus far
23. 86.4%
24. still open
25. 23%

Average=30.2%

increased costs than does friendly adjustment. This does not seem to be the situation involved in other fields of extra-judicial settlements.

In the bankruptcy system creditors' rights are protected throughout. The general problem of fraud has previously been discussed. Creditors, or their legal representatives, are permitted to force the examination not only of the debtor and his wife, but by Section 21A of the Bankruptcy Act, of "any designated person". Such examinations of course, are best conducted by experienced lawyers. They are carried out with the force and effect of law, *i.e.,* in court, under oath, etc. Any other method would seem to be little short of worthless. That such examinations are often not productive of the desired results should not minimize their importance. The system is so designed that by an involuntary petition, and the use of the receiver, the property may immediately be put in the charge of the court for the benefit of all creditors. The preferential four month period for the benefit of all creditors leads to involved law suits and legal services, only because it is necessary to protect creditors. Frequently it results in the creation of a substantial estate where at first little or nothing appeared.

The system was also designed to be protective of the bankrupt's rights. It grants him a discharge. It provides him an attorney's fee. It allows him exemptions. A system guaranteeing such important rights, privileges, powers and immunities is expensive. The friendly adjustment system also claims the power to give a "contract" discharge,[92] if the creditors conclude the bankrupt is worthy of one.[93] But here we meet the same difficulty which was encountered in the original decision as to whether or not the bankrupt's "honesty" was such as to warrant the bureau's retention of the case. What standard shall be selected for determining whether the bankrupt is deserving of the discharge? The mere whim of the creditors'—their possible desire to let loose their anger against the insolvent himself, anger engendered, possibly, by short-sightedness in having extended credit to such an inefficient (fraudulent) business man? The friendship adjustment scheme has no yardstick.

The Bankruptcy Act, on the other hand, defines and sets up a standard for which a refusal of a discharge may be made. Its legal interpretation may be difficult, but it is necessary. The importance of a legal discharge granted to the deserving—*i.e.,* "honest" in the

[92]Billig, *What Price Bankruptcy: A Plea for "Friendly Adjustment", supra* note 2, at 438.

[93]*Ibid.* 438, n. 60.

legal sense—insolvent debtor is not to be measured in dollars and cents.[94] Purely from the bankrupt's point of view, it would seem that a conscientious advisor should not recommend friendly adjustment unless at least the three major rights of an attorney's fee, discharge, and statutory exemptions were assured him. These matters have been hitherto practically unmentioned in considering the problem, yet they seem to have a direct relation to public policy.[95] It may be conceded that a system that deprives both creditors and debtors of such privileges and rights is bound to cost less.[96] But wise business men do not always choose the cheaper article.

Again, it should be pointed out that generally speaking, the officials and their duties created by the Bankruptcy Act have their parallel under the friendly adjustment plan. The receiver and trustee, the chief liquidating officers in bankruptcy, have their counterpart in the bureau liquidator; the receiver and trustee's attorney in the bureau's attorney. Both systems employ appraisers, accountants, custodians and auctioneers whenever needed. The fact that in broad aspects each system structurally resembles the other indicates that practically all of these offices, or duties, are essential to any systematic, orderly, estate liquidation. They may be changed in small particulars, *i.e.*, one appraiser may be substituted for the required three.[97] But these

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[94]See Levinthal, *The Early History of Bankruptcy Law* (1917) 66 U. OF PA. L. R. 224. In the Yale New Jersey study, out of 1,000 cases studied, objections to discharges were filed in 50. In only 5 of these, discharges were refused; in 33, the discharge was granted nevertheless, and 12 were still open.

[95]See report, IN THE MATTER OF AN INQUIRY, ETC., *supra* note 7, at 177, quoting from an address of Referee Geo. A. Marston of Detroit: "The debtor very often does not receive any release from his obligations and after the distribution is...forced into Bankruptcy in order to get a discharge..."

In the 25 friendly adjustment Newark cases studied, 4 went to the Bankruptcy Court. Of the remaining 21, 1 debtor received his statutory exemptions. In these same 21, releases were granted in 8, not granted in 1, and "not yet" in 12.

[96]"The administration of bankrupt estates in England is as expensive as, if not more than, the So. District of New York. The examination of the debtor's conduct and affairs is far more careful and painstaking, and much of the expense is incurred on that score." Article appended to report, IN THE MATTER OF AN INQUIRY, ETC., *supra* note 7, at 306.

"The examination of the debtor's conduct and affairs independent of the wishes of the creditors and independent of the size of the estate is a most salutary feature of the Act. It is undoubtedly expensive." *Ibid.* 308.

[97]*Ibid.* 58; Billig, *Extra-Judicial Administration of Insolvent Estates, supra* note 2, at 320; Douglas and Weir, *op. cit. supra* note 90, at 20.

small differences do not make for basic superiority so far as costs of administration regarding officers are concerned.

If in fact friendly adjustment seems to be able to do the work cheaper, it is not essentially because it lessens the officers nor because it has a simpler structure, but because the work required of these officers (which in a large number of cases seems to be absolutely necessary) is reduced to a minimum and is not so valuable. The one important item of saving is that it does away with the intermediary court designed to furnish protections and safe-gnards to creditor and debtor alike. These protections and safe-gnards against dishonest debtors, against dishonest and preferred creditors, of discharges, exemptions, examinations,—may or may not be considered as "necessary", if they are, they are factors in determining what is the "superior" system.

To those who claim, especially in the small bankruptcy case, that the value of the article would appear to be too small to insure by the "cumbersome" methods of bankruptcy, the reply should be that the "dividend return" should not be measured in dollars and cents, but rather in the fact that no cost is too high to have thorough protection and investigation of the debtor, his wife, relatives, friends and other creditors. The discussion on this point merely suggests the necessity of some type of summary procedure in bankruptcy for small cases,[88] similar to the English practice, the size of the estate only to be determined by further research, not necessarily that bankruptcy be discarded entirely in favor of friendly adjustment.

Because of the large group of creditors, however, who are willing to sacrifice the investigations and safe-guards of the bankruptcy machinery for the sake of salvaging as much as possible, from their investment (and it is not entirely strange that business men should be so inclined) the wise suggestion has been made for another government official, a paid examiner or investigator for all cases.[89] This is so be-

[88]See Billig, *Extra-Judicial Administration of Insolvent Estates, supra* note 2, at 316. Aso see *supra* note 81.

"It has seemed that in large estates there should be given to the creditors the right to select their own trustee....The difficulty is to draw the line between what are small and what are large estates, since the schedules based upon the opinion of the bankrupt are liable to vary largely from the amounts actually realizable." Report, THE MERCHANTS' ASS'N. OF NEW YORK, *supra* note 10, at 74.

[89]*Ibid.* 57-67, where a paid Auditor and Examiner is recommended, to be a permanent official investigating all cases. It would be of particular importance in the no-asset cases, where the estate can not afford to bear adequate investigations. At present, it is better for debtors to come in with no assets than with

cause there are elements of policy in every case that transcend mere considerations of dividend returns.[100] A salaried government investigating official would present the two-fold advantage of permitting larger dividend returns by not forcing the bankrupt estate to bear this part of the costs of administration, and nevertheless of insuring a thorough investigation, especially in the cases listed as no-asset and very small asset.

The distressing fact is that so many business men divorce themselves from these considerations. They do not insist upon strictly enforcing the discharge or criminal provisions of the Act,[101] and expose themselves and the entire business community to further exploitation through fraud or inefficiency by unheedingly permitting bankrupts to set themselves up in business again. This leads to the conclusion that such duties in the interests of public policy, should fall upon the Government itself.[102] The present Bankruptcy Act, deficient in so many of these considerations, in thousands upon thousands of cases, at least partially offers some such advantages and checks. But friendly adjustment seemingly disregards the entire problem and swings completely to the opposite extreme. Is one system "superior" to the other? The difficulty of replying is obvious.

It should also be pointed out what can be done by way of low cost of administration under the Bankruptcy Act. The bankruptcy figures of Detroit show that expenses only very slightly higher than under friendly adjustment can be obtained. This would seem to indicate

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an estate that would support investigation, for the Bankrupt who comes in with assets may thereby "hang" himself.

In England, it is the duty of the Official Receivers to examine all cases.

Also, see report, IN THE MATTER OF AN INQUIRY, ETC., *supra* note 7, at 43. where a Federal Bankruptcy Commissioner is recommended, one of whose duties would be the investigation of small asset cases.

[100]"The aim [of the English Act] was not so much to give creditors the largest possible returns in each individual case as to prevent occurrence of dishonest failures generally." *Ibid.* 36.

Also see memorandum, *Ibid.*

[101]See editorial, *Bankruptcy Evils,* New York Sun, Aug. 26, 1930.

[102]"The central purpose of the English Act was to make bankruptcy a difficult and disagreeable process and so far as possible to weed out from the business community corrupt and incompetent traders." IN THE MATTER OF AN INQUIRY, ETC., *supra* note 7, at 36.

"We should have the principle followed in England. That principle is that the enforcement of discipline is a public matter, that it cannot be left to the initiative of scattered creditors, but must be effected through centralized government machinery." *Ibid.* 37.

that bankruptcy probably has come in for some unjust criticism as to the costs of administration which are really necessary to keep the wheels of the system moving in efficient fashion.[103]

CONCLUSION

It is practically impossible to judge any two systems that differ so greatly in the number of cases handled. No fair comparison can be made between the tens of thousands of cases that run through the bankruptcy mill and the comparatively few selected cases turned out by the bureaus. If the bureaus were subjected to the same barrage of no-asset, small asset, and complicated-situation cases that bankruptcy must administer, comparisons might more fairly be hazarded. Any such statement as that credit men "now adjust *a vast number* of merchant insolvencies" in their "own commercial forum,[104] therefore, when compared with the number turned out in bankruptcy, is slightly misleading.[105]

On the whole, it is not denied that friendly adjustment seems capable of furnishing larger dividends to creditors than does bankruptcy. If this is the business man's sole consideration, then he should choose this means of liquidation. But the inability of bankruptcy to duplicate this particular feat should not be considered a result of "flaws in the present system". Any system that simply marshals the assets, sells them, and distributes the remains to creditors, must necessarily be more generous in dividends. Query, why cannot so-minded creditors informally appoint anyone to perform these simple services and thus further increase their dividends by

[103]Special local conditions, however, may account for these low Detroit figures: Because of such local conditions, the Committee, (*Ibid.* 95) reported "...relative administration expense in different districts cannot be taken as a measure of efficiency, because of variable factors (rents, etc.) which also include the size of the cases involved". It goes on to say, however, "complete receivership administration, which is the rule in Detroit, does not necessarily involve added expense to estates, but under proper direction, should mean reduced expense through greatly reduced rentals".

[104]Billig, *Extra-Judicial Administration of Insolvent Estates, supra* note, 2, at 317. (Italics are the writer's).

[105]In the fiscal year selected for comparisons in certain Districts, 1284 cases were liquidated in friendly adjustment, and 17,927 were closed in Bankruptcy. "More than 110,000 Bankruptcy cases were concluded in the years, 1928, 1929." IN THE MATTER OF AN INQUIRY, ETC., *supra* note 7, at 35. The 25 Newark cases analyzed above represents the bulk of such work done there in the past two years. There are 68 such bureaus.

saving even the 10% bureau fee? But these considerations are not essentially an attack against the present system. It is merely claiming that such a method is cheaper than any well designed bankruptcy act can be. Thus, the statement that "the success of friendly adjustment is partially dependent upon the existence of a National Bankruptcy Act *which has deficiencies*"[106] is also misleading. It would rather seem to be dependent upon the existence of *any* well-designed bankruptcy act. In other words, no serious attempt is here made to "defend" the present Bankruptcy Act. In certain of its phases it is past defending.

But creditors should first realize the significance of their choice, *i.e.*, what they are losing before they accept such a substitute system. Speed and salvaging a few extra dollars from the wreck, the two considerations in which friendly adjustment certainly excels, are only two of many important considerations.[107] Bankruptcy at least affords a method of legal supervision, innumerable checks, prohibitions, and protections. Friendly adjustment on the other hand liquidates with a delightful informality.[108] It would be interesting to study the cases that have been liquidated by the bureaus merely to ascertain the number of preferences that possibly lie hidden in them, and that could have been set aside in bankruptcy; or how many of the pit-falls of the "composition" are prevalent in its non-technical easy-going procedure. It is a fertile field for those who hitherto have had to make their plans with due regard to the bankruptcy prohibitions.

There is not the slightest doubt, however, that there are many cases that would lend themselves to the friendly adjustment type of

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[106]Billig, *Extra-Judicial Administration of Insolvent Estates, supra* note 2, at 318, (Italics are the writer's).

[107]"Bankruptcy administration [in England] is not cheap; nor is it speedy. It is efficient in the realization of assets, in the investigation of the conduct and affairs of the debtor, and in the exclusion from trade of persons whose activities have been shown to be a menace to honest and fair dealing in the commercial life of the community." Article appended to report, IN THE MATTER OF AN INQUIRY, ETC., *supra* note 7, at 308.

[108]Referee George A. Marston of Detroit, in an address to the National Association of Referees in Bankruptcy, described the liquidation of insolvent estates under a trust mortgage (which is used in some states instead of assignments) as "the grand climax of looseness of administration. There is no control over administration here whatever. The trustee disposes of the property for whatever price he thinks best; pays whatever expenses he wishes, and if there is anything left, distributes it to creditors". *Ibid.* 177. "Our correspondence with Judges, Referees and Attorneys contain much criticism of the methods adopted by...associations outside of bankruptcy." *Ibid.* 176.

settlement. Possibly some plan might be devised whereby, even under the Bankruptcy Act, this form of liquidation could be employed, so as to combine the advantages of both. But it should be realized that bankruptcy as a system has been subjected to many false and exaggerated criticisms; that many of the grounds upon which it may with justice be adversely criticised are equally applicable to the substituted system advocated. The principal point is that the few simple details accomplished in any kind of "friendly adjustment" admittedly can be done more easily and therefore more cheaply than the more intricate operations necessary to any well-designed Bankruptcy Act.