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In Spring 2009, after decades of challenges and years of hemorrhaging money, Chrysler and General Motors filed bankruptcy within weeks of one another, thereby initiating two of the most notorious bankruptcy proceedings of all time. Filed against the backdrop of the global financial crisis that came to a head in fall of 2008 and simultaneously the transition from the George W. Bush Presidential Administration to that of Barack Obama, the automaker bankruptcies were unique for their combination of size, speed, and high political profile. These two cases pushed prior bankruptcy law and practice to their limit and, as many have argued, well-beyond, into the realm of lawlessness. Indeed, the controversy did not end with the successful emergence of the companies from bankruptcy in 2011. It still remained a vital issue in the 2012 Presidential election, with some believing that President Obama's support for the auto bailouts and subsequent intervention in the bankruptcy proceedings contributed positively to his re-election that year.

The cases have spawned reams of analysis by judges, law professors, economists, politicians, and even participants in the high-profile cases. Yet the unique historical, political, and economic context of the cases has also led to great uncertainty as to their long-term impact on bankruptcy doctrine and practice, and the extent to which the cases should be treated as merely one-off *sui generis* cases or valid precedents shaping future law. The decision of the Supreme Court of the United States to subsequently vacate the Chrysler decision further confounds matters. Still, a leading critic of the Chrysler decision has argued that the case has already borne fruit in the controversial decision to approve the reorganization plan of the City of Detroit. Finally, supporters of the government's intervention—most notably from former President Barack Obama—have seen the cases as both an economic and, perhaps more importantly, political success, because these cases have raised the possibility that despite the dubious legality of the cases, political leaders might look to the cases in the future as a template for similar interventions in other industries, especially those involving powerful political interest groups.

This essay will review the course of the automaker bankruptcies to assess these cases' long-term legal, economic, and political impacts on bankruptcy law and practice. However, in the assessment of the cases, a crucial analytical distinction must be kept in mind throughout the entire discussion that follows: namely, the distinction between the narrow case for *some* limited government intervention to facilitate what could have otherwise been relatively ordinary bankruptcy cases, versus what *actually* transpired cases, which essentially became a political free-for-all that may have actually reduced the effectiveness of the long-needed company reconstruction.[1] Indeed, as will be seen, the majority of the most controversial and troubling aspects of the cases had little to do with the actual economic and financial reorganization of the companies. However, analyses of the cases tend to conflate these two issues, treating the cases as essentially all-or-nothing, take-it-or-leave-it packages of multiple different financial and political elements. Distinguishing these two basic elements is essential, however, to assessing the long-term lessons of the cases.

I. THE DESCENT INTO BANKRUPTCY

The road to the Chrysler and GM bankruptcies was many years in the making, but was precipitated by the financial crisis that rocked global markets in 2008. The impact of that crisis not only shaped the descent of Chrysler and GM into bankruptcy, but also was crucial to the debate over the unprecedented role of the United States government in its decision to intervene in the cases in the first place.

A. The Prelude to Bankruptcy

The descent of Chrysler and General Motors into bankruptcy was long in coming and resulted from decades of mismanagement, uncompetitive employee wage and benefit structures, and failure to adjust to the changing consumer demand and foreign competition. Moreover, as illustrated by the contrary experience of Ford, bankruptcy was far from inevitable.

In 1980, for example, General Motors possessed 45% market share in the U.S. auto industry. By 2009, however, that number had shrunk to 19.5%. Over this period, Ford and Chrysler also suffered erosion of market share. Yet much of the cost structure and dealer network of the U.S. 'Big Three' in the auto industry was set during those high-flying years, including extremely generous wage and benefit contracts. Goolsbee and Krueger, who participated in the auto bailouts as members of the Obama Administration, report that the hourly compensation of workers at the Big Three automakers was almost 25% higher than for transplants.[2] After including the legacy costs of retirees, they estimate that average labor costs for the Big Three were almost 45% higher. They conclude that the only way for American automakers to become competitive would be to reduce the fixed costs associated with retirees, the uncompetitive compensation levels for existing workers, and the heavy interest payments that they owed to bondholders.

Moreover, American automakers struggled with extraordinarily uncompetitive, collectively-bargained labor contracts that were a legacy of flush times. For example, under collectively-bargained UAW contracts, laid-off workers received 95% of their normal pay. Because union employees were effectively paid the same no matter they worked or were idle, labor was effectively a fixed cost for the firms.[3] 'With fixed costs so high, they had an incentive to build as many cars as possible so as to reduce the average cost per car. Similarly, with variable costs relatively low, additional cars could be made without much additional expense.'[4] These peculiar incentives led the automakers to focus on increasing output and sales volume, which in turn led to their extreme dependence on discounts and incentives to sell unwanted cars. As Rattner concludes, 'The end result was what no businessperson would want—a low-margin business that is vulnerable to any slackening in consumer demand.'[5] Also, this heavy fixed-cost structure made the American automakers particularly vulnerable to demand fluctuations over time.

In addition, UAW workers had the opportunity to retire at an early age and the UAW was notorious for its generous retiree benefit plan, which essentially provided free medical and dental care and prescriptions for life.[6] In 2007, Chrysler agreed to create a Voluntary Employee Beneficiary Association ('VEBA'), which was directly provided and funded by the auto companies and would assume responsibility of retiree health care benefits. Under the plan, Chrysler was committed to make a one-time \$8.8 billion contribution to the VEBA, and in return it would have no further obligation. Thus, if the \$8.8 billion turned out to be inadequate to fund the VEBA, responsibility for the shortfall would rest on the shoulders of the VEBA–UAW and the workers.

By the time of the financial crisis that began in 2008 and the ensuing recession, both GM and Chrysler were in dire financial straits. In 2007, GM lost \$40 billion and suffered losses of \$15 billion in the first three quarters of 2008.[7] Market share fell precipitously for both GM and Chrysler during that time as well. Despite their massive losses, both companies repeatedly claimed that it was not realistic for them to file bankruptcy because doing so would scare off consumers who would fear that they would not have their warranties honored and their cars serviced.[8] As a result, they insisted that the only option was a taxpayer-funded bailout and that bankruptcy was not a viable option to save the companies. Indeed, at the time when GM first approached the government for a bailout it had expressly refused to make contingency plans for a bankruptcy filing if no bailout was forthcoming.[9] As Steven Rattner subsequently observed, the refusal to make preparations for bankruptcy 'would add materially to the cost of the eventual rescue.'[10]

By the end of the process, American taxpayers had committed $81.8 billion total to auto-related bailouts.[11] This includes $49 billion to GM, $12 billion to Chrysler, $1.5 billion to Chrysler Financial, over $17 billion to GMAC (General Motors Acceptance Corp.), $600 million to support the consumer warranties on GM and Chrysler vehicles during the bankruptcy processes, and $400 million to supply-chain providers of auto parts (although $5 billion was committed only $400 million was drawn).

GM and Chrysler's failure and subsequent demand for bailouts contrasted with the actions of Ford during that same period.[12] Ford had suffered many of the same market dynamics as GM and Chrysler during that period. Unlike their rivals who were beset by poor management and inability to reform internally, Ford's management underwent a painful internal restructuring from 2006. It sold off non-core product lines such as Land Rover, Aston Martin, and Jaguar, unlike GM and Chrysler. Therefore, Ford did not end up having to file bankruptcy.

B. The Dubious Legality of Using TARP Money for Auto Bailouts

The legality of using TARP money to bail out the auto companies has been highly contested. Steven Rattner reports that when GM first lobbied the White House seeking to have TARP funds provided to bail out the auto companies, then-Secretary of the Treasury Hank Paulson opined that TARP was 'intended to stabilize the financial system, not bail out industrial companies.'[13] He then reportedly added, 'You're note going to be able to use it. . .. You will probably need to go to Congress.'[14] Paulson's skepticism was well-founded, as subsequent analysis by law professor Gary Lawson of the statutory text and authority granted by the TARP concluded that despite the extreme vagueness of the statute, the TARP legislation permitted those funds to be used only for 'financial institutions,' not car companies.[15]

Consistent with Paulson's admonition, the auto makers turned to Congress for a grant of bailout funds. Perhaps the most obvious evidence that the TARP was not intended to be used for the auto bailouts is the fact that Congress actually felt that it was necessary to consider separate legislation on the question of bailing out the automotive industry. As noted, that legislation passed the House of Representatives in December 2008, only to fail in the Senate. Had Congress believed that it had already authorized TARP funds to bail out the auto industry, it seemingly would have been unnecessary to consider special legislation doing just that. In fact, following President Bush's decision to allocate TARP funds to the automotive industry, irate Senators who had just voted down the very action then taken by the President sent a sharp letter to the President stating that 'Congress never voted for a federal bailout of the automobile industry, and the only way for [TARP] funds to be diverted to domestic automakers is with explicit congressional approval.' Ironically, the measure failed in the Senate because the appropriation lacked adequate safeguards to protect the bill from turning into a pure bailout that would not have required the automakers to engage in greater restructuring of UAW wages and benefits to bring them into parity with transplant automakers, a measure pushed by Senator Bob Corker of Tennessee, a state with numerous auto transplant factories.[16] The UAW refused the demand for wage concessions as a concession for receiving taxpayer money. As with GM itself, whose refusal to prepare for a bankruptcy filing was a game of chicken designed to force the Bush Administration into a bailout, the UAW refused concessions knowing that even if the negotiations in Congress failed, the Bush Administration would likely provide a bailout anyway in the short-run, which left the UAW to revisit the issue under the incoming labor-friendly Obama Administration.[17]

Once the measure failed in Congress, however, President Bush announced the unilateral diversion of TARP funds to the automakers. But he did not provide any legal justification for that decision.[18] Although the use of TARP funds was challenged by some of Chrysler's creditors, the bankruptcy court ruled that they lacked standing to raise the claim. The Supreme Court subsequently ruled all further challenges to be moot.

C. The Road Not Taken

Many assessments of the wisdom and efficiency of the auto bailouts conflate two distinct elements of the issue.[19] In so doing, the analysis obscures clear understanding of the nature of the controversies those cases engendered.

The first option that the government could have followed would have been to provide financing to the auto companies in order to effectuate their reorganization, either directly or through a guarantee to a private lender, but otherwise allow the bankruptcy process to proceed in an ordinary fashion according to the established rules and priorities of the bankruptcy process. This intervention in the process could have been extremely limited at addressing the continued disruptions in credit markets that had begun in 2008 and persisted through the period of the auto bailouts. Under this targeted intervention, the government's limited and passive role would have enabled the bankruptcy judge to pursue the ordinary goals of a bankruptcy proceeding—restructuring the firms' operations and balance sheet to maximize financial viability going forward.

The second option, which the government pursued instead, was to leverage the limited need for assistance to credit markets in order to provide debtors in possession financing to alter the bankruptcy process and accomplish other goals, such as to pursue politicians' political goals or to alter bankruptcy practice and priorities to advantage politically-powerful stakeholders in the bankruptcy process. In particular, under this more interventionist approach, the bankruptcy-bailout combination permitted politicians and interest groups to pursue aggressive redistributive and political goals instead of narrow economic goals. In a sense, the government was able to use the limited need for assistance to stabilize credit markets as a wedge into the cases that subsequently opened up very large opportunities to accomplish other goals.

The essence of bankruptcy reorganization turns on a distinction between two concepts: financial distress and economic failure.[20] In turn, these concepts turn on whether a firm is fundamentally worth more alive than dead—i.e., whether the current deployment of the human, physical, and financial capital assets kept together as a going-concern is worth more than the opportunity cost of those assets if the firm was liquidated and redeployed elsewhere in the economy.

Under this fundamental bankruptcy analysis, normally GM would have been the prototype for a firm that would be easily reorganized in bankruptcy, as it was clearly financially distressed rather than economically failed. Despite its longstanding struggles, it seems obvious that GM was worth more as a going-concern, at least in some configuration, than it would have been had it been liquidated and its assets redeployed elsewhere in the economy. These assets included a highly skilled workforce, firm and industry specific physical equipment and plants, several valuable models and nameplates with high consumer loyalty, and the potential for a positive cash-flow business that could provide returns to investors who invested. In this conventional analysis, GM was an easy case for bankruptcy reorganization. Under normal circumstances, it could have filed bankruptcy and reorganized without much difficulty. Indeed, similar reorganizations are commonplace in the American economy today: department stores, hotels, and even airlines, all are consumer-facing industries that have had numerous bankruptcy filings in recent years.

By contrast, Chrysler presented a more difficult call as to whether it was merely financially distressed or economically failed. An economically failed firm is one for which the current deployment of human, physical, and financial capital is lower than the opportunity cost of redeploying those assets elsewhere in the economy. As the smallest of the Detroit Three, Chrysler was in the weakest competitive position to remain viable going forward as an independent concern. Moreover, analysis by the Obama Administration suggested that much of Chrysler was in direct competition with other American automakers, especially GM, for market share. As a result, one likely consequence of Chrysler's liquidation would have been to strengthen GM's competitive position as it was poised to pick-up much of Chrysler's lost sales.[21] According to Steven Rattner, one option that was considered regarding Chrysler was a merger with GM. In the end, of course, Chrysler's assets were sold to the Italian automaker Fiat, a result which was consistent with the notion that the company was not viable as a stand-alone entity going forward.[22]

Where a firm is merely financially distressed, an efficient chapter 11 bankruptcy reorganization can restructure the balance sheet so as to create positive cash flow for the firm and to pay pre-bankruptcy creditors more than they would receive if the firm was liquidated instead. It follows from this positive cash-flow position that for such a firm, post-bankruptcy debtor in possession financing should be readily available to the firm. With respect to an economically failed firm, however, the lack of a viable path to solvency and viable cash flow going forward makes such loans highly risky.

This analysis suggests that, under normal circumstances, certainly GM and probably Chrysler would have been able to attract debtor in possession financing to fund their reorganization proceedings. However, at the time of their insolvency in late-2008 and early-2009, credit markets were still not functioning effectively, which suggested that they might have been unable to attract short-term credit because of liquidity conditions in markets, not because they were fundamentally failed as economic enterprises. If this were so—and there is little evidence to support or contradict the claim other than the self-serving testimony of Bush and Obama Administration officials—this reality could have arguably supported a limited role for government intervention to unclog credit markets. In that case, the government arguably could have stepped forward with limited and targeted debtor in possession financing, or even to merely guarantee private investment, which would have delivered the needed capital to reorganize the firm.[23] For example, at the time, future Republican candidate for President Mitt Romney argued that it would be appropriate for the federal government to 'provide guarantees for post-bankruptcy financing and assure car buyers that their warranties [were] not at risk.'[24] If this strategy had been pursued, the government could have limited itself to providing short-term, targeted financing but otherwise allowed the bankruptcy process to run its ordinary course.

Instead,the government chose the alternative path of a comprehensive intervention and aggressive control of the bankruptcy reorganization process. Seizing on the alleged need for a guarantee of debtor in possession financing or direct provision of financing, the government used that as a wedge to exert active control over the whole process, including controversial steps to arguably rearrange established bankruptcy priorities, to change the firms' management and dictate the firms' business plans and priorities, to strong-arm creditors into going along with the government's schemes, to reward and protect powerful political allies, and to accomplish political goals that had little to do with furthering GM and Chrysler's economic viability going forward and in many ways impeded it. As discussed in greater detail below, these decisions included large wealth transfers to members of the United Auto Workers union to protect them from the typical pain of bankruptcy, protection of politically-powerful auto franchise dealers from being closed, and the use of the government's influence to incentivize the increased production of environmentally friendly vehicles by Fiat-Chrysler, independent of the economic efficiency of that business strategy.

Contrary to standard bankruptcy analysis, these interventions and others like them—i.e., protecting the UAW from significant wage reductions, protecting inefficient dealers from downsizing, and providing incentives to manufacture unprofitable small cars—did *not* aid GM and Chrysler in reorganizing to become more viable as competitors. Instead, they did exactly the *opposite*—each of these interventions, which were imposed upon the firms and the bankruptcy judge by the government, actually *reduced* the going-forward economic competitiveness of the firms by limiting their discretion to make the necessary cost adjustments and improvements that would have made them more effective competitors over the long run. In other words, far from helping to save or reorganize the companies, these particular elements of the auto bailouts were like barnacles strapped to the companies' hull that they were forbidden to remove and instead continued to drag down their efforts to effectively reorganize.

The government thus confronted two different paths. On one hand, the government could have provided a limited intervention targeted to address the particular problem of poorly-functioning credit markets that otherwise would have provided liquidity to the firms, thereby leaving the basic bankruptcy process intact and focusing on reorganizing the companies into more efficient and viable competitors. On the other hand is the path actually pursued by the government—to use the limited need for assistance to provide liquidity to capital markets to drive a process heavily focused on *redistributive* and *political* goals and not merely the economic viability of the firms themselves. By pursing this path instead, the government implicitly chose to subordinate the goals of economic efficiency and competitive to multiple other goals that contradicted those goals.

This analysis suggests that an important threshold conceptual point to keep in mind in assessing the auto bailouts is that, simply because there it might have been efficient for a limited government intervention to address the problems in credit markets, that does not necessarily imply that it is necessary to accept all of the political and redistributive elements of the case as efficient as well.

The Obama Administration has justified some of its decisions, such as the preferential treatment afforded to the UAW, as appropriate to advance efficiency goals of reorganization because the failure to do so could have led the UAW to strike, thereby resulting in the liquidation of the companies. In particular, the Obama Administration's decision in the Chrysler case to provide debt and equity to the underfunded UAW health care VEBAs while leaving the secured creditors incomplete was justified by the alleged fear that a failure to do so could prompt UAW workers to strike, thereby leading to the collapse of the companies; or as Rattner writes, 'you need workers to make cars.'[25]

Yet neither Rattner nor any other member of the Auto Task Force provides any evidence to support the assertion that career GM and Chrysler employees would strike the companies into liquidation instead of accepting wage and benefit concessions that would bring them into line with foreign transplants but still far exceeded the wages of most U.S. manufacturing workers. Moreover, in other analogous cases where unionized workers have been asked to take wage and benefit reductions, such as in airline bankruptcy cases, I have located no instances where workers have responded to demands for wage and benefit reductions by striking the company into liquidation. The Administration's willingness to take this assertion at face value and require no concrete justification is especially striking in light of the Auto Task Force's hardline approach to creditors, where the government rejected as implausible the creditors' claim that they would walk away instead of taking the government's offer. To the extent that the government's justification for favoring retired UAW workers over other retirees (including the Indiana teachers and police retirement funds) relates to the purported need to prevent UAW workers from striking, that justification appears to be somewhat specious and unsupported. Thus, as discussed below, this decision to spare UAW workers much of the pain absorbed by other stakeholders in the case appears to pit against one another the two contrary goals of economic efficiency and the desire of the Administration to reward a powerful political interest group.

II. THE BANKRUPTCY CASES

Chrysler filed its bankruptcy cases in the Southern District of New York on April 30, 2009, before Bankruptcy Judge Alberto Gonzalez. GM filed its bankruptcy on June 1, 2009, and the case was assigned to Bankruptcy Judge Robert Gerber. Although the two cases differed significantly due to the differences between Chrysler's and GM's situations at the time, the cases are very similar in many ways, including certain important aspects.

A. Chrysler

1. The case

On April 30, 2009, Chrysler LLC and 24 of its domestic subsidiaries filed bankruptcy. According to the bankruptcy court, in calendar year 2008 Chrysler recorded revenues of $48.5 billion, with assets of approximately $39.3 billion and liabilities of $55.2 billion.[26] As a result, Chrysler's net loss was $16.8 billion in 2008 alone.

When Chrysler filed bankruptcy, 80.1% of the equity of Chrysler Holding LLC (Chrysler's parent) was owned by Cerberus Capital Management, L.P. and its affiliates, and 19.9% was owned by Daimler AG. Chrysler also had several different groups of creditors. The largest one was approximately $6.9 billion, which was owed to a syndicate of lenders and secured by a first-priority security interest in substantially all of Chrysler's assets. Chrysler also owed $2 billion to affiliates of Cerberus, secured by a second-lien security interest in those same assets. In addition, Chrysler owed $4.27 billion to the U.S. Treasury Department in connection with the loan it received from the TARP in the prior fall, which was secured by a first-priority lien on any unencumbered Chrysler assets and the inventory of Chrysler's MOPAR parts division, as well as a third-priority lien on any assets already encumbered with first and second priority liens. Chrysler also had approximately $5.34 billion in unsecured trade debt. Finally, Chrysler owed $10 billion to a voluntary employee benefit association ('VEBA') that had been established in 2008 to provide healthcare benefits to union retirees.[27]

Chrysler filed a pre-packaged bankruptcy plan. Under the proposed plan, the old Chrysler sold substantially all of its operating assets to a newly-formed entity, New CarCo Acquisition LLC ('New Chrysler') for $2 billion in cash from New Chrysler and its assumption of some liabilities of old Chrysler (including the obligations owed to the VEBA). The $2 billion that was received was distributed to the first-priority secured lenders, who thus received about 29 cents on the dollar for the $6.9 billion that they were owed, and consuming all of the revenue from the asset sale. This left no assets for the second or third priority lienholders for unsecured creditors. The first-priority creditors also received no unsecured deficiency claim and existing equity holders received nothing.

New Chrysler's asset purchase and operating expenses were financed by $6 billion in new secured credit from the U.S. Treasury from the TARP. The Canadian government also provided financing to New Chrysler's Canadian affiliate. The U.S. Treasury also received an 8% equity stake in New Chrysler and the Canadian government received 2%.

Most of the newly-issued equity in New Chrysler, however, was issued to two parties that provided no cash to New Chrysler. The majority position—55% — was provided to the VEBA. Along with $1.5 billion in cash and an unsecured note for $4.6 billion, this equity, cash, and debt replaced the $10 billion unsecured debt owed to the VEBA. Finally, Fiat S.p.A. was initially issued 20% of New Chrysler's equity but could receive 'up to 35%' of the equity of New Chrysler in exchange for providing technology (primarily related to the manufacture of smaller, fuel-efficient vehicles), distribution, and other things to Chrysler, if certain performance metrics were met, including fuel-efficiency metrics.

2. The criticisms

The rushed and irregular procedures followed in the Chrysler case has resulted in widespread criticism and confusion regarding the precedential implications for future bankruptcy cases. Because of the basic structural similarities between Chrysler's and GM's cases, many of the criticisms are consistent across the two; but distinctions between the two cases also raise particular issues unique to each case.

As a matter of bankruptcy law and policy, the Chrysler case occasioned greater controversy and concern than the GM case, not only because it was filed first but also because some controversial features of the Chrysler plan that were absent in the GM case. Those criticisms can be captured under three basic headings.[28] First, Chrysler and GM broke with established bankruptcy law and practice: the two cases essentially permitted the effective reorganization of the entire companies through the mechanism of a sale of the whole company, rather than proceeding through the standard practice of a Chapter 11 reorganization process. In addition, the ostensible sale terms also explained how the proceeds of the sale would be distributed, rather than following the priority scheme laid out by the Bankruptcy Code. The comprehensive nature of the sale and dictating of the distribution of the proceeds, it is argued, constituted the equivalent of a plan of reorganization or a so-called *sub rose* plan. Second, even if the sale was appropriate in general, the process used to conduct the sale—and in particular the lack of competing bids—was highly irregular.

Finally, the plan itself provided that, not only would secured creditors fail to receive full payment on their claims but also unsecured creditors with junior priority—the UAW VEBAs—would receive larger distributions in the case (44 cents on the dollar of their claims) than the secured creditors (which would receive only 29 cents on the dollar). In the following part of this chapter, I examine each of those claims in turn.

a. Was the Chrysler case a sub rosa plan of reorganization? From a bankruptcy perspective, the cornerstone of the Chrysler and GM cases was the novel use of sections 363 and 1129 of the bankruptcy code, which authorizes the debtor to sell assets as part of the bankruptcy case. Section 1129 permits the debtor to sell assets as part of a confirmed plan of reorganization. Section 363(b), by contrast, permits the debtor to sell assets and only requires the approval of the bankruptcy court after notice and hearing, and it does not require a confirmed plan of reorganization for the sale. As a practical consequence, this means that a §363 sale can be conducted much more rapidly and without the myriad procedural protections of a sale as part of a confirmed reorganization plan. Over time, it has become more common to sell the debtor's assets pursuant to §363 while distributing the proceeds of the sale to creditors in accordance with the Code's priority scheme.

Although §363 sales have become a more common element of bankruptcy cases, the sales in the Chrysler and GM cases was nevertheless highly irregular and controversial. First, the sale was unusual in that the entire sale process was essentially orchestrated to favor one bidder (the United States government) and did not invite competing bidders that could have bid up the price of the company for the benefit of creditors. In addition, no competing estimates of the value of the company's assets were solicited. Second, the sale was also irregular in that the purchaser was not a new arms'-length owner, but was essentially a continuation of the preexisting company and management that remained almost identical. Third, the purported sale was controversial in that the proceeds were not distributed in accordance with the priority scheme of the code but that as a condition of the sale dictated that preference should be provided to the UAW VEBA's unsecured claims instead of the secured claims of bondholders.

More generally, it has been argued that the assets sales in both cases were not really merely asset sales at all but rather de facto or *sub rosa* plans of reorganization, as they sold essentially all of the debtors' assets as a going concern and provided a distribution and priority scheme for the proceeds. As David Skeel has demonstrated, the Bankruptcy Code's Chapter 11 reorganization rules were designed to prevent the sort of arrangement that Chrysler (and later GM) would follow.[29] As Skeel observes in the early

20th century, 'large troubled corporations did not file for Chapter 11 like they do today. They used a process known as "equity receivership," which involved an artificial "sale" of the company to a new entity set up by the debtor and the investment banks who represented its bondholders and stockholders.' Moreover, like the Chrysler case, 'The new entity was the only bidder at the sale, and creditors who were unhappy with the terms of the reorganization had very little opportunity to interfere.'

Skeel notes that the use of a §363 sale had become common at the time of the auto bankruptcies. But Chrysler was distinct from this sales in that there was effectively no competitive bidding and that the 'sale' also included within it seeming alterations to bankruptcy priority rules by giving certain unsecured creditors (namely the UAW VEBA plans) a substantial stake in New Chrysler, while largely freezing out existing creditors. As Skeel writes, 'What makes the Chrysler plan unique, and makes it similar to the receiverships of the New Dealers' era, is that it is not really a sale at all. It is a pretend sale and its main purpose is to eliminate the pesky creditors who might otherwise interfere with the government's plan.'[30]

During the New Deal, therefore, the Bankruptcy Act was amended to address these practices. In particular, a more transparent and inclusive reorganization process was mandated to prevent insider enrichment and safeguards against unfair treatment were issued. Although some of the more stringent provisions were relaxed in the Bankruptcy Code, the modern bankruptcy process still places limits on what can be done through a §363 sale and requires large-scale restructuring in bankruptcy to be conducted according to the Chapter 11 process.

Permitting the debtor to conduct a sale of virtually all of the debtor's assets, especially when combined with dictates on the distribution of the proceeds that alter the Code's priority scheme, can enable a debtor to avoid all of the Code's built-in procedural protections within the Chapter 11 plan process, including the disclosure, voting, and plan confirmation requirements. As a result, courts have consistently held that they should be vigilant to ensure that a purported asset sale does not amount to 'sub rosa plan' that effectively resolves a case in the fashion of a confirmed plan of reorganization but without the procedural protections of that section.[31]

In the Second Circuit, where the Chrysler case was filed, the prevailing law was provided by the *Lionel* case, decided in 1983.[32] Under *Lionel*, a court can permit an asset sale outside the ordinary courts of business if there is legitimate business reason for the sale. In the *Chrysler* case, the bankruptcy court found that Chrysler's proposed asset sale would preserve Chrysler's going concern value, which was a good business reason for approving the proposed §363 sale.[33] In particular, the bankruptcy court concluded that the proposed transaction was the only viable alternative to liquidation of the company, because despite extensive efforts to find alternatives, no other option had been forthcoming. Moreover, the unusual speed of the sale was justified because several of Chrysler's factories were closed pending resolution of the case and Chrysler was burning through cash, resulting in an ongoing reduction in Chrysler's going-concern value.

b. Procedural requirements: competitive bidding and valuation According to the bankruptcy court, the sale of Chrysler for $2 billion was warranted because the company was valued at zero to $800 million, according to expert testimony presented at the case. As a result, the Obama Administration claimed that the $2 billion paid by the taxpayers to purchase Chrysler's assets was actually substantially more than the market price of the company, which is also a highly contested claim.

According to Roe and Skeel, the initial valuation submitted by Chrysler's experts gave a range of $900 million to $3.2 billion, with a likely recovery to the first liens of between $654 million and $2.6 billion,[34] which was subsequently revised downward to reflect changing conditions with the passage of time.[35] Moreover, although it is true that the experts retained by Chrysler presented the only valuation to the court, this is likely because the court did not provide objecting creditors with sufficient time to present an alternative valuation from their experts or provide for a competing valuation that would be paid for by the bankruptcy estate.[36] As a result, the court only received evidence from Chrysler's valuation expert and only with respect to the limited valuation scenarios described therein.

As to the inference that the absence of competing bids indicates that the government's plan was the only viable plan for Chrysler, this ignores the highly irregular nature of the bid solicitation process in the case. Indeed, as Roe and Skeel observe, 'The courts' deference to the sale proponents' weak market test was the single most disturbing feature of the Chrysler bankruptcy.'[37] In particular, they argue that in light of the tainted nature of the consent of a majority of the creditors because of their TARP entanglements, the lack of competing valuation opinions and the large uncertainty of the valuation opinion provided, and the fact that the court was circumventing the procedural protections of a standard Chapter 11 case by approving a sale that was effectively a reorganization, it was particularly important for the court to provide a market test. As they argue, '[T]he market test was the key way by which the Chrysler plan could have fully justified itself, removing the taints. But it did not.'[38]

However, the requirements that had to be met to qualify as a competing bidder were novel and conditioned on multiple conditions that had nothing to do with maximizing the value of competing bids or revealing Chrysler's underlying value. As David Skeel observes,

> The government proposed that no bid be allowed unless the bidder promised to protect precisely the same favored creditors as were protected by the government's bid. In Chrysler, for instance, bidders would be required to assume the approximately $5.3 billion of trade claims and offer stock and a nearly $4.6 billion note to retirees. A bidder could not simply bid, say, $2.5 billion, for Jeep, even though such a bid would provide more proceeds than the government's bid.[39]

To be a qualified bid, any competing bids had to promise to assume Chrysler's collective-bargaining agreements and products liability claims as well.[40] Douglas Baird has similarly observed that by only permitting bids that valued Chrysler as a going-concern, the court foreclosed potentially higher bids that would have contemplated a piecemeal sale of Chrysler, including the separate sale of Jeep and various real estate holdings.[41] 'In short,' Baird argues, 'the key question in Chrysler is not that there was a sale, but enough was done to look at sales that took different forms.'[42] As Roe and Skeel observe, the case was merely 'marketing valuations of the bankruptcy plan actually used, one that didn't separate Chrysler's assets from its largest preexisting liabilities. As such, their efforts were efforts to market the plan they preferred, not the alternative plans the Code requires the court to test.'[43] Moreover, the Court only gave competing bidders a week to place bids, which made it difficult to conduct due diligence or obtain financing for a bid.[44] Given the irregular nature of the case, Roe and Skeel argue that the court should have been especially vigilant to require a 'robust market test, not a weak one.'[45]

c. Did the plan violate absolute priority? Perhaps the most controversial element of the Chrysler bankruptcy case was the potential violation of the absolute priority rule, a standard bankruptcy principle that typically requires senior creditors to be paid in full before any distributions are made to junior creditors. In the Chrysler case, it was proposed that secured creditors with senior priority would be paid only 29 cents on the dollar on their claims, while the claims of the UAW's VEBA were paid at approximately 44 cents on the dollar.

According to the *Chrysler* bankruptcy court, however, the proposal did not violate absolute priority because the UAW supposedly would not be receiving any payments on account of its pre-petition claims against Old Chrysler.[46] Instead, the payments to the VEBA arose from new value provided to *New* Chrysler to facilitate the reorganization and from negotiations between the VEBA and New Chrysler. According to the bankruptcy court, therefore, the transfer of this new value to the VEBA 'was neither a diversion of value from the Debtors' assets nor an allocation of the proceeds from the sale of the Debtors' assets.'[47] The Second Circuit eventually affirmed the conclusion that all of the money paid to the UAW VEBA was from new value, not in payment of the UAW's prepetition claim. As a result, the proposal did not violate bankruptcy priority rules and did not constitute a *sub rosa* plan as it was not an effort to override the Code's priority scheme.

Steven Rattner has also argued that the preference for junior creditors was justified by new value exception to the absolute priority rule, which awards discretion to those who provide new funds to a bankrupt company to direct those funds as they see fit. Rattner argues that the new value exception justified the government's decision to give away Chrysler's equipment to Fiat for nothing except the provision of technology and management.[48] The Administration also pointed to the fact that even though warranty holders were unsecured claimants as well, they received full payment, as did many suppliers, and that there was a valid business reason for treating the UAW VEBA accordingly.[49]

One unusual aspect of the case was the willingness of Chrysler's secured bondholders to consent to their treatment in the case instead of fighting the government's proposal. This consent came about through an unusual process. Under the terms of their credit agreement, the first-priority secured lenders agreed to appoint an administrative agent who had authority to represent the creditors as a group and the creditors agreed to be bound by the actions that the agent took as instructed by a majority of the indebtedness in the case.[50] In the Chrysler case, 92.5% of the indebtedness supported the agent's actions; as a result, the trustee's release of the lender's liens in the case were determined to be binding on the first-priority secured lenders.[51] On the other hand, while the vote of the creditors' trustee outside might be binding outside bankruptcy, it is not clear that should bind parties within bankruptcy, where the Code provides its own voting rules.

The willingness of so many creditors to go along with the Chrysler plan is puzzling at first glance in that much of Chrysler's debt was held by substantial and sophisticated financial institutions, such as JPMorgan. This peculiarity might have several explanations. First, a large amount of Chrysler's debt was held by a number of large financial institutions that had received TARP funds from the government, and thus were unusually vulnerable to political pressure from Washington. Citigroup, JPMorgan Chase, Goldman Sachs, and Morgan Stanley—which together received $90 billion in bailout funds from the U.S. Treasury—held 70% of the dollar amount of the claims against Chrysler.[52] In addition to the direct leverage provided by the TARP, those banks also faced other governmental pressures, as the government was actively considering nationalizing some or all of them and displacing their management. As Roe and Skeel observe, 'Bank executives had reason to be wary, as Treasury-induced management changes of compensation mandates were being discussed. Senior bank management had good reason not to annoy the Treasury.'[53] Some critics of the cases have argued that because of their compromised positions they lacked the ability to vote independently, which is problematic in that through their votes they were able to bind other creditors who were not similarly compromised. Some commenters have gone so far as to argue that the votes of those bondholders should be disqualified because of their compromised position or that they should have been segregated into a separate class for voting purposes.[54]

In an additional extraordinary twist, President Obama and the White House intervened to strong-arm and intimidate nonconsenting bondholders to compromise their positions. President Obama held a nationally televised press conference where he excoriated those holders of Chrysler secured debt who refused to accept the government's treatment that provided them with 50% less of distribution than junior unsecured debt.[55] In addition, one investor claimed that the White House threatened to 'destroy its reputation' by turning the White House press corps against the bank if they did not drop their opposition.[56] Notably, among those who objected to the Administration's treatment and the §363 sale included the pension plans for the Indiana State Teachers and Police retirement funds, who eventually appealed the case all the way to the Supreme Court.[57]

According to the Administration, the arrangement in the Chrysler case did not violate the absolute priority rule because in receiving 29 cents on the dollar on their claims, the secured creditors received all that they were properly entitled to in bankruptcy—namely, the liquidation value of the company's assets.[58] As noted above, however, no independent valuation or competitive bids for the company's assets were permitted in the case.[59]

In addition to alleging that the plan violated the absolute priority rule, Chrysler's senior creditors had another complaint, namely that since they were not paid in full on their secured claims in the case they should have been entitled to a deficiency claim as an unsecured claim in the case as well. Instead, they were provided with a secured claim of 29 cents on the dollar but received nothing on the additional 71 cents that seemingly should have been paid as an unsecured claim even though the UAW VEBA received approximately 44 cents on the dollar for their unsecured claim. But the Bankruptcy Code requires that reorganization plans must be fair and equitable to all parties, which among other things requires that similarly-situated creditors be treated similarly. Thus, it seems to follow that even if they did not receive full payment on their secured claims, the bondholders should have received an unsecured deficiency claim for the remainder.[60] The bankruptcy court rejected this argument on the basis that, because the money that was transferred to the UAW came from new value provided by the government to New Chrysler and was not on account of the UAW's claim against Old Chrysler, the secured creditors had no right to those funds, nor could they complain of unfair discrimination.

B. General Motors

1. The case

GM filed bankruptcy on June 1, 2009, when GM employed approximately 235,000 employees worldwide. Among the 91,000 employed in the United States, 61,000 employees were represented by the UAW.[61] As of March 31, 2009, GM had reported assets of approximately $82 billion worldwide and liabilities of $172 billion.

Among GM's liabilities was $19.4 billion owed to the U.S. Treasury under the TARP, which was secured by a first-priority security interest in intellectual property, real property, cash, and equity, and a second-priority security interest in other assets. Unlike Chrysler, most of GM's debt was unsecured, amounting to approximately $117 billion, including $21 billion owed to GM's UAW VEBA and over $27 billion in outstanding bonds. GM also owed $3.9 billion to a group of creditors led by Citicorp US, Inc., $1.5 billion to a group led by JPMorgan Chase, $400 million to Export Development Bank Canada, and $125 million to Gelco Corporation. Those loans were secured in part by GM's inventory, equipment, and equity. Upon filing bankruptcy, GM received debtor in possession financing from the U.S. Treasury ($30.1 billion) and the Canadian government ($3.2 billion with $6 billion to be provided later).

The basic structure of the GM bankruptcy followed that of Chrysler. A newly-formed entity named Vehicle Acquisition Holdings LLC ('New GM') purchased almost all of Old GM's assets and assumed some of its liabilities, most notably the obligations owed to UAW VEBA. In exchange, new GM issued 10% of its common stock to Old GM and two separate warrants to purchase 7.5% of the post-closing outstanding shares of New GM at different levels of equity valuation. The U.S. Treasury and EDC, which had lent over $50 billion to GM in combined pre-petition and post-petition secured financing, assigned their loans to new GM, which then credit bid for the assets of Old GM.

New GM then issued 60.8% of its common stock to the U.S. Treasury, along with $2.1 billion of its preferred stock, and a $6.7 billion note. To EDC, GM issued 11.7% of its common stock, $400 million of its preferred stock, and a $1.3 billion note. Other first-priority secured lenders of Old GM (other than the U.S. Treasury and the Canadian government) were repaid their $6 billion in full by New GM. Curiously, therefore, secured creditors of Old GM were paid in full—unlike the secured creditors in Chrysler, which received only 29 cents on the dollar. Unsecured creditors received from Old GM the 10% equity stake in New GM, an additional 2% of New GM's stock if general unsecured claims against Old GM exceeded $35 billion, and the warrants to purchase an additional 15%. Old GM's shareholders received nothing. As part of the plan, the UAW agreed to make concessions to New GM on employee compensation and benefits and on retiree healthcare. Moreover, the plan proposed to create a new UAW VEBA, which would provide 17.5% of New GM's common stock, $6.5 billion in preferred stock, and a 6-year warrant to acquire 2.5% of New GM's common stock.

GM's plan had many of the same essential characteristics as Chrysler's. According to the bankruptcy court in GM's case, the sale again was warranted as it concluded that the only alternative to the §363 sale was liquidation and that the estate would benefit from a quick §363 sale; therefore, there was an adequate business reason to support the proposed sale.[62] Nor was the bankruptcy court persuaded that the sale amounted to a *sub rosa* plan, as the sale did not alter creditor priorities and that creditors received the full amount to which they were entitled.

One striking distinction between the Chrysler and GM cases is that whereas the secured creditors in Chrysler received a major haircut, Old GM's secured creditors were paid in full. There is no obvious reason why secured creditors were treated differently in the two cases, leading to the supposition that the differential treatment was one of convenience, rather than principle—that in Chrysler, which had a large amount of secured debt, it was necessary to stiff secured creditors in order to ensure adequate funds were available to transfer to the UAW, whereas in GM, the amount of secured debt was relatively small and as a result it was not necessary to squeeze secured creditors in order to transfer wealth to the UAW.

2. The criticisms

Many of the criticisms of the GM case are similar to those in the Chrysler case and will not be rehashed here—most notably the claim that the sale of the entirety of GM's assets as a going concern, without truly competitive bidding, and the instructions on how to distribute the proceeds, constituted a *sub rosa* plan. Moreover, because GM's plan paid secured creditors in full, it did not raise the issues of possible violation of the absolute priority rule in order to make payments to the UAW VEBA. Most of GM's bondholder debt was unsecured, not secured, and thus of equal priority at the UAW.

On the other hand, GM's plan proposed to pay a much larger percentage of the unsecured claims of the UAW VEBA than the unsecured claims of the company's bondholders. This implicated a different provision of the Bankruptcy Code, the requirement that creditors of similar priority should be treated similarly and not suffer unjust discrimination. Under this principle, it is presumptively the case that all creditors of similar priority—such as all general unsecured creditors—should share equally in the pro rata distribution of the estate's assets. Instead, the unsecured claims of the UAW VEBA received a much higher percentage distribution than the unsecured bondholders, who received about 10 cents on the dollar.

C. The Precedential Value of the Chrysler and GM Bankruptcies

The Chrysler and GM bankruptcies raised multiple novel issues of bankruptcy law and policy and broke substantial new ground with respect to the question of the degree to which debtors could use the procedure of a §363 sale to circumvent the process and protections of Chapter 11.[63] After the Second Circuit affirmed the Chrysler sale, a group of disappointed creditors petitioned the United States Supreme Court to stay the sale pending appeal. After initial hesitation and issuance of a stay, the Supreme Court refused the request for a stay and allowed the sale to proceed.[64]

After the stay was denied, the objecting creditors eventually returned to the Supreme Court and asked it to review the case on the merits. The Supreme Court responded by first granting *certiorari* on the case but then remanded the case to the Second Circuit with instructions to dismiss the appeal as moot.[65]

The Supreme Court's unusual action of granting certiorari and then dismissing the case as moot—instead of merely refusing the grant of certiorari in the first place—is significant for understanding the precedential role of the cases. This unusual procedural gambit effectively has only one important effect—by first accepting the case for certiorari this had the effect of vacating the lower court's opinion approving Chrysler's sale, thereby vacating its precedential value. It is therefore unclear what the continued precedential value of the cases is and whether they are valid to be relied upon in future cases.

In its short opinion, the Supreme Court cited *United States v. Munsingwear, Inc.*[66] Joseph Warburton notes that *Munsingwear* stands for the proposition that taking a case on certiorari and dismissing it as moot is done 'to prevent a judgment, unreviewable because of mootness, from spawning any legal consequences.'[67] By doing so, the action 'clears the path for future relitigation of the issues between the parties.'[68]

III. THE ROLE OF POLITICS

A defining element of the auto bailouts was the important role played by politics throughout the process. Times of economic and financial crisis are times in which the rule of law is most needed but also most likely to be relaxed in the face of political pressure and seizure of authority by the government to engage in discretionary decision-making.[69] Relaxing the rule of law can provide discretion to government officials to respond positively to emergent, unexpected problems; on the other hand, relaxing the rule of law can provide a rent-seeking opportunity to interest groups and politically-opportunistic politicians. Government-driven bailouts, such as those of banks during the financial crisis or the auto companies, invariably will be riddled with political bargains designed predominantly to further redistributive and political goals rather than economic efficiency.[70]

The political dynamics of the auto bailouts may be best summarized in a comment by South Dakota Senator John Thune to GM and Chrysler executives once they received government funding, 'You find yourself with a board of directors of essentially 535 members.'[71] At the same time, the auto companies found themselves responding to the particular political desires of the Obama Administration—namely the desire for greater production of green and smaller cars—regardless of effect of those policies on the bottom line. In turn, Democratic politicians were seeking to protect and reward political allies from organized labor, auto dealerships, and other interest groups.[72] The overall effect of these political pressures was to interfere with the bankruptcy and to weaken the needed restructuring of the companies.

The most notable beneficiary of the auto bailouts was the UAW. Indeed, as noted, the bankruptcy court concluded that the funneling of money to the UAW VEBA's instead of secured creditors did not violate the absolute priority rule because all of the funds that the government provided post-petition were designed specifically to enrich the UAW, without any claim that the UAW was entitled to those funds on account of its preexisting claim.

In fact, analysis by James Sherk and Todd Zywicki concluded that the entirety of the taxpayers' losses on the Chrysler and GM cases was attributable to preferential treatment given to the United Auto Workers in the bankruptcy cases as compared to similarly-situated parties in analogous cases, such as airline bankruptcies.[73] In all, Sherk and Zywicki estimate that the subsidies transferred to the UAW amounted to $26.5 billion, greater than the $23 billion loss that taxpayers suffered as a result of the bailouts. Most notably, the UAW's underfunded health care plans were treated far better than other unsecured creditors in similar cases.

Moreover, mechanics and airline pilots have been forced to make wage concessions to bring them into line with prevailing market rates in order to make the firm competitive. In the auto bailouts, by contrast, existing UAW workers were asked to make minimum concessions, as all pay cuts were to be borne by new hires. Steven Rattner later admitted, 'We asked all the stakeholders to make very significant sacrifices. We should have asked the UAW to do a bit more. We did not ask any UAW member to take a cut in their pay.'[74] In his memoir of the experience, he states that he 'felt a little bit of buyer's remorse about the Chrysler-UAW contract,' and that the failure to take a harder line in the Chrysler case had been a missed opportunity to increase Chrysler's overall competitiveness.[75] Beyond the direct transfers to the UAW's underfunded health care plans the Obama Administration's auto task force even approved the diversion of $1 billion of bailout money to 'top off' the pensions of the UAW members at the bankrupt auto parts manufacturer Delphi, which had been spun off from GM years before GM's bankruptcy and was merely one of many GM parts suppliers. At the same time that the auto task force transferred funds to Delphi, the auto task force forced the termination of the pension plan for Delphi's white collar workers and pointedly refused to include in its largesse blue-collar members of smaller, less-powerful unions.[76] And while these various transfers aided UAW members and retirees it should be remembered that among the holders of Chrysler's secured bonds were the Indiana police and teachers pension funds, thus the case may have been one of simply transferring wealth from a group of retirees with less political clout to one that was more powerful.

The cases were also characterized by a substantial amount of political meddling by Democratic members of Congress seeking to protect and enrich favored local interest groups and constituencies. Most notably, although a primary purpose of the bankruptcy filings was to enable GM and Chrysler to trim their overextended dealer networks, members of Congress intervened to aggressively protect auto dealers in their various districts.[77] Other politicians pressured the companies for special treatment for home-state suppliers of raw materials or intervened to prevent the closure of certain manufacturing facilities.[78] These interventions on behalf of politically-powerful interests were counterproductive to the companies' efforts to reduce costs and improve their competitive position.

IV. THE AFTERMATH

The auto bankruptcies were no ordinary bankruptcy cases and the implications of the cases have resonated well beyond that of the typical bankruptcy case. The legacy of the Chrysler case has turned out to be particularly contentious as a result of the controversy surrounding the decision to pay secured creditors less than in full while simultaneously providing the unsecured claims of the UAW VEBA with 50% more than secured creditors received, which arguably violated the absolute priority rule.

A. Effect on Credit Markets

The criticism of that element of the Chrysler case was immediate and heated.[79] Warren Buffett, for example, warned that it would 'disrupt lending practices in the future.'[80] He stated, 'If we want to encourage lending in this country, we don't want to say to somebody who lends and gets a secured position that that secured position doesn't mean anything.'

Empirical studies of the long-term impact of the Chrysler case have produced mixed results. Anginer and Warburton examined the impact of the Chrysler case on bond market prices for highly unionized companies and found no evidence that the Chrysler case led to higher risk premiums for bonds issued by heavily unionized companies.[81] Subsequent analysis by Blaylock, et al., by contrast, found that firms in more unionized industries experienced lower event-window abnormal bond returns, higher abnormal bond yields, and lower cumulative abnormal bond returns.[82] The authors also found that those effects were greatest for firms that are closer to distress.

B. Effect on the Automotive Industry

Since the auto bailouts, the Big Three automakers have recovered well and returned to profitability. Supporters of the government's actions point to the auto bailouts as a cause of this development. Another unusual aspect of the auto bailouts was the Obama Administration's decision to seize the opportunity to engage in government industrial planning, especially with respect to its emphasis on using the leverage of the bailouts to push for increased manufacturing of smaller cars, as exemplified by the decision to essentially give Chrysler to Fiat in exchange for small-car technology and the built-in financial incentives for Fiat to increase the average gas mileage of Chrysler's fleet. In one famous exchange on the verge of bankruptcy, President Obama asked his advisors 'Why can't they make a Corolla?'[83] Astonishingly, his advisors replied 'We wish we knew.'[84]

In reality, the explanation as to why American automakers 'can't make a Corolla' is quite simple—because the high labor costs of Detroit automakers renders doing so infeasible to manufacture smaller cars such as Corollas, i.e., high-volume, low-margin cars. The problem of high cost was exacerbated by the persistent gap held by consumers in the perceived quality of American products and that of the imports. Thus, Steven Rattner reported that a GM 'premium compact' sold for $3,814 less than a Toyota, 'a stunning gap for car prices at less than $20,000.'[85] And whereas 77% of Toyota's cars were on the 2009 *Consumer Reports* recommended list, only 21 of GM's cars made the list, and *zero* of Chrysler's offerings.[86] As Rattner concluded,

> [A]s much as the Detroit Three had been pilloried for missing the small-car market, their failure wasn't due to complete stupidity. If it costs $1,000 more in extra labor expenses to build a car that could be sold for only $16,000—nearly $4,000 less than its competitor—it would be impossible to make a profit. So why build it?[87]

Given this, it is not surprising that of the best-selling cars (excluding light trucks) in the United States, the most popular ones are Japanese cars, including (in order) the Toyota Camry, Honda Civic, Toyota Corolla, Honda CR-V, Toyota RAV4, Honda Accord, Nissan Rogue, Nissan Altima, all before any American car appears on the list (the Ford Escape).[88]

However, this ignores a more important story—the top-three best-selling vehicles in the United States are three pickup trucks: the Ford F-Series, Chevrolet Silverado, and RAM Trucks. And although Toyota sold 360,000 Corollas in the United States in 2016, Ford sold 820,000 F-Series trucks, making it the best-selling consumer vehicle in the United States for the 35th year in a row.[89] In contrast, in 2016 GM sold 24,739 Chevy Volts, despite major tax incentives.[90]

In short, to the extent that the American automakers have returned to profitability following the auto bailouts, it is precisely because they *ignored* the pressure of the Obama Administration to try to manufacture Corollas and other small cars, but instead have prospered by building larger, higher-priced vehicles where Detroit's higher labor costs can be recouped by higher prices. In addition, an extended period of low interest rates on car (and other) loans (thereby making more expensive cars more affordable) and low gasoline prices have made consumers more willing to purchaser those vehicles. This suggests that the efforts of the Obama Administration to use the bankruptcy process as an opportunity to engage in larger industrial planning may have been misguided.

C. Other Effects

The auto bankruptcies have also had effects that ripple beyond their particular impacts on credit and auto markets. Many of these effects have been completely unexpected but suggest the complexity of containing the full reach of such a dramatic action.

David Skeel has argued that effect of the courts' approval of the controversial aspects of the Chrysler case was to pave the way for even more dramatic actions in the city of Detroit's bankruptcy case in 2013. The controversy in the Detroit case focused on the disposition of the art and other assets of the historic Detroit Art Museum that were owned by the city. Under standard principles of bankruptcy, the DAM's art collection would have been sold for maximum value in order to pay off the claims of the city's creditors. In that case, however, the court supervised a 'Grand Bargain' that provided that the museum's collection be purchased and donated to a private trust, with the funds to be provided by a combination of state funding and private contributions. This would enable the collection to be maintained intact and retained in the city of Detroit. In turn, the funds received by the bankruptcy estate would be earmarked to pay the claims of the city's retirees and pensioners, rather than distributed to general creditors.[91]

As David Skeel observes, the Grand Bargain 'cleverly' resolved two of the key issues in the case. 'The only concern with the Grand Bargain,' he notes, 'was that it did not appear to be legal.' Moreover, he points to the Chrysler and GM sales as the conceptual foundation of the scheme, 'relying as they did on a fictitious sale that was designed to favor some groups of creditors over others.'[92] In fact, he adds, 'With both of its key features, the fictitious sale and the favoring of one group of creditors, the Grand Bargain was in some respects even more audacious than Chrysler or GM.'[93] He concludes, 'Indeed, it seems unlikely that the Grand Bargain would ever have been tried if it were not for the carmaker bailout precedent.'

Another unexpected issue that arose from the auto bailouts related to the use of the government's leverage *after* the bankruptcy filing was completed but while the U.S. Government still owned a controlling stake in Ally Financial, formerly GMAC, the vehicle finance arm of GM.[94] In addition to transferring TARP funds directly to GM and Chrysler, the government's bailout plan also provided funds to GMAC and Chrysler Financial (which later merged into Ally) and took a majority ownership stake in Ally. One of the major new institutions created by the Dodd-Frank Financial Reform legislation was the creation of the Consumer Financial Protection Bureau, which inherited enforcement responsibilities for fair lending laws. One early priority of the CFPB was to pursue claims of alleged racial discrimination against auto dealers and auto lenders. The CFPB chose Ally Financial as one of its first major targets.

According to a report of an investigation by the House Financial Services Committee, the CFPB chose Ally as one of its first cases not because Ally had done anything provably wrong or was particularly egregious in its behavior, but among other reasons because the government held 73.8% of the bank (and still held 63.4% at the time the case was actually settled).[95] The government's control of Ally placed it in a particularly weak position to fight a different arm of the federal government. For that reason, along with others, Ally was unable or unwilling to fight the federal government and settle the case. In addition, Ally needed regulatory approval from other governmental agencies that the CFPB was able to hold up.[96] As a result, Ally capitulated, eventually paying $98 million.

A final issue regarding the long-term legacy of the auto bailouts was the scandal involving GM's ignition switch litigation. One of the key provisions in the approval of the bankruptcy plan by the court was the provision that the 'sale' to New GM would be free and clear of all claims. Under normal circumstances, this provision would prevent creditors that could have brought their claims prior to the bankruptcy from doing so after the bankruptcy against the purchaser of the assets. All creditors, including tort creditors, whose claims arose prior to the bankruptcy case, would normally be required to assert those claims against the estate of the bankrupt debtor (Old GM) and would not be able to assert those claims against the new owner.

In March 2014, however, New GM announced for the first time that there were serious defects in the ignition switches used in many of their cars that could result in accident, property damage, personal injury and even death.[97] The defective parts had been installed going back to the 2005 model year and had persisted during the period that the U.S. government owned GM. As of the time of the litigation to determine whether those claims could be asserted against New GM, over 140 class action cases had been brought for the defective parts and the overall economic loss was estimated to run from $7 billion to $10 billion.

The Bankruptcy Court had originally barred many of the claims from going forward against New GM, holding that they arose from actions taken prior to the bankruptcy case and thus should be asserted against Old GM. On appeal, however, the Second Circuit held that because GM knew about or should have known with reasonable diligence the flaw before it filed bankruptcy and did not provide notice, customers' claims survived the bankruptcy filing.[98] As the Second Circuit wrote, 'New GM essentially asks that we reward debtors who conceal claims against potential creditors. We decline to do so.'[99] In addition, the Court specifically rebuked GM for not bringing the matter to light during the period of the government's ownership of the company.[100]

V. CONCLUSION

As a result of the unprecedented intervention of the U.S. government, the bankruptcy cases of Chrysler and General Motors pushed bankruptcy law to the limit, and many would say beyond. Absent the federal government's interference, the cases themselves raised no inherently novel or unusually difficult issues—they could have proceeded as conventional Chapter 11 cases. General Motors would have almost certainly reorganized successfully, with a new capital structure, more realistic labor agreements, a leaner dealership network, and shorn of money-losing product lines. The fate of Chrysler, the smallest of Detroit's 'Big 3' automakers, was less certain, but the eventual acquisition of the company Fiat was one plausible scenario. With respect to the unique circumstance of their filings having occurred at the height of the financial crisis, the federal government arguably could have played a role in providing liquidity directly to the companies or in guaranteeing a private lender's extension of capital to make that possible.

Instead, the federal government launched an intervention that was unprecedented in its scope and unprecedented in the challenges that it raised to bankruptcy doctrine. The cases challenged core bankruptcy practices, such as the traditional requirements for fair sales processes as well as the distribution of sales proceeds. Although the sales were upheld by the bankruptcy courts and Courts of Appeals, when the Chrysler case finally reached the Supreme Court the Justices took the cases on *certiorari*, thereby dismissing the cases, only to immediately dismiss the case as moot. As a result, the continued legal validity of the actions taken in those cases remains open to question.

Despite the continued questions regarding their legal authority, the real-world consequences of the Chrysler and GM bankruptcies is unquestionable. Not only did the approval of the cases enable the companies to go forward, the courts' decisions arguably played a role in Barack Obama's successful 2012 re-election campaign, and the creative nature of the plans arguably served as a crucial precedent in the later bankruptcy filing by the City of Detroit. Finally, for one of the first times in American history, the cases introduced a new notion of 'political risk' into otherwise predictable bankruptcy proceedings, creating ripple effects across the economy. While the short-term consequences of the cases are now complete, the long-term story is yet to be written.

NOTES

1. *See* Todd Zywicki, *The Corporatist Legacy of the Auto Bailouts*, Liberty Law (January 13, 2014), http://www.libertylawsite.org/2014/01/13/the-corporatist-legacy-of-the-auto-bailouts/.; Todd J. Zywicki, *The Auto Bailout and the Rule of Law*, 7 Nat'l Affairs 66 (Spring 2011).
2. Austin D. Goolsbee & Alan B. Krueger, *A Retrospective Look at Rescuing and Restructuring General Motors and Chrysler*, 29 J. Econ. Persp. 3 (2015).
3. Paul Ingrassia, Crash Course: The American Automobile Industry's Road to Bankruptcy and Bailout—and Beyond 7 (2011). In fact, unemployment benefits were so generous that eventually they gave rise to the phenomenon known as 'inverse layoffs,' in which senior workers volounteered to be laid off (at 95% salary) and thus bumped junior workers back onto the assembly line. *Id.*
4. Steven Rattner, Overhaul: An Insider's Account of the Obama Administration's Emergency Rescue of the Auto Industry 87 (2010).
5. *Id.*
6. *Id.* at 153.
7. *See id.* at 20.
8. *Id.* at 23.
9. *Id.* at 27. One reason for refusing to make bankruptcy preparations might have been to ensure a messy bankruptcy if no bailout was forthcoming, thereby essentially creating a moral hazard problem or chicken game to force the government's hand on a bailout.
10. *Id.*
11. *Id.* at 297.
12. *See id.* at 205–7.
13. *Id.* at 23–4.
14. *Id.*
15. *See* Gary Lawson, *Burying the Constitution Under a Tarp*, 33 Harv. J.L. & Pub. Pol'y 55 (2009). *But see* Congressional Oversight Panel, September Oversight Report: The Use of TARP Funds in the Support and Reorganization of the Domestic Automotive Industry 4 (2009) (noting that the legality of the auto bailouts was subject to 'considerable debate' and that there was 'ambiguity' in the legislative language and congressional intent).
16. *See* Rattner, *supra* note 4, at 35–7.
17. *Id.* at 38.
18. *See* Lawson, *supra* note 15.
19. Goolsbee and Krueger, for example, assume that accepting the wisdom of a government role for financing in the auto bankruptcies implies that one must accept the full range of government activity in the cases. *See* Austin D. Goolsbee & Alan B. Krueger, *A Retrospective Look at Rescuing and Restructuring General Motors and Chrysler*, 29 J. of Econ. Perspectives 3 (2015).
20. *See* Zywicki, *Auto Bailout*, *supra* note 1.
21. *See* Goolsbee & Krueger, *supra* note 19.
22. Douglas Baird has claimed that the sale to Fiat was really a way of 'allow[ing] Chrysler to fail slowly over the course of several years in a way that coincided with Fiat's entry into the U.S. market,' instead of closing Chrysler immediately. *See* Douglas G. Baird, *Car Trouble* 4 (Univ. of Chi. Law & Econs., Olin Working Paper No. 551, 2011). 'With luck,' he writes, 'Fiat could make its cars at factories that had been producing Chryslers while taking advantage of part of Chrysler's existing distribution system.'
23. *See* Zywicki, *Corporatist Legacy*, *supra* note 1.
24. Mitt Romney, *Let Detroit Go Bankrupt*, N.Y. Times, Nov. 18, 2008, at A35.
25. *Id.*
26. *In re* Chrysler Llc, 405 B.R. 84, 89 (Bankr. S.D.N.Y. 2009).
27. *See* A. Joseph Warburton, *Understanding the Bankruptcies of Chrysler and General Motors: A Primer*, 60 Syracuse L. Rev. 531 (2010).

28. A useful summary of these and other issues in the Chrysler case can found in Mark J. Roe & David Skeel, *Assessing the Chrysler Bankruptcy*, 108 Michigan L. Rev. 727 (2010).
29. David Skeel, *Why the Chrysler Deal Would Horrify a New Dealer*, The American (May 8, 2009).
30. *See also* Ralph Brubaker & Charles Tabb, *Bankruptcy Reorganizations and the Troubling Legacy of Chrysler and GM*, 2010, U. of Ill. L. Rev. 1375 (2010) (arguing that the structure of the GM deal was similar to that of the equity receiverships that courts eliminated during the late-19th century).
31. *See* Pension Benefit Guar. Corp. v. Braniff Airways, Inc. (*In re* Braniff Airways, Inc.), 700 F.2d 935 (5th Cir. 1983).
32. Comm. of Equity Sec. Holders v. Lionel Corp. (*In re* Lionel Corp.), 722 F.2d 1063 (2d Cir. 1983).
33. *In re* Chrysler Llc, 405 B.R. 84, 96 (Bankr. S.D.N.Y. 2009).
34. *See* Roe & Skeel, *supra* note 28, at 742 n.39.
35. *Id.* at 742.
36. Chrysler's expert was paid $10 million to prepare its opinion. *See* Baird, *supra* note 22.
37. Roe & Skeel, *supra* note 28, at 746.
38. *Id.*
39. David A. Skeel, Jr., *From Chrysler and General Motors to Detroit*, 24 Widener L.J. 121 (2015).
40. Roe & Skeel, *supra* note 28, at 747.
41. *See* Baird, *supra* note 22, at 13.
42. *Id. See also* Barry E. Adler, *A Reassessment of Bankruptcy Reorganization After Chrysler and General Motors*, 18 ABI L. Rev. 305; Roe & Skeel, *supra* note 28.
43. Roe & Skeel, *supra* note 28, at 747.
44. *Id* at 749.
45. *Id.* at 748.
46. *In re* Chrysler Llc, 405 B.R. 84, 99 (Bankr. S.D.N.Y. 2009).
47. *Id.*, 405 B.R. at 99.
48. *Id.*
49. *Id.* at 181.
50. *Id.* at 96.
51. Warburton, *supra* note 27, at 543.
52. *See id.* at 552.
53. Roe & Skeel, *supra* note 28, at 743.
54. *See* Adler, *supra* note 42, at 310; Roe & Skeel, *supra* note 28, at 744.
55. *See* Rattner, *supra* note 3, at 178. President Obama made similar statements against GM's bondholders that objected to their treatment.
56. *See* Warburton, *supra* note 27, at 552.
57. *See id.* at 544.
58. Rattner, *supra* note 4, 180. Rattner argues that even though the $2 billion that Chrysler's secured creditors received as less than the face value of their loans 'it represented more than 100 percent of the Chrysler's assets, as the company's liquidation value indicated.'
59. Warburton, *supra* note 27, at 543.
60. *See id.* at 555–6.
61. *In re* General Motors Corp., 407 B.R. 463, 475 (Bankr. S.D.N.Y. 2009).
62. *Id.* at 491–3.
63. There has been some debate over how novel the GM and Chrysler cases were. *Compare* Stephen J. Lubben, *No Big Deal: The GM and Chrysler Cases in Context*, 83 Am. Bankr. L. J. 101 (2009) (not novel) *with* Mark J. Roe & Joo-Hee Chung, *How The Chrysler Reorganization Differed from Prior Practice*, 5 J. of Legal Analysis 400 (2013).
64. Ind. State Police Pension Tr. v. Chrysler, LLC, 129 S. Ct. 2275 (2009).
65 . Ind. State Police Pension Tr. v. Chrysler, LLC, 130 S. Ct. 1015 (2009).
66. United States v. Munsingwear, Inc., 340 U.S. 36 (1950).

67. Warburton, *supra* note 27, at 575–6 (quoting *Munsingwear*, 340 U.S. at 41).
68. *Id.* at 576 (quoting *Munsingwear*, 340 U.S. at 40); *see also* Fred N. David, *Interpreting the Supreme Court's Treatment of the Chrysler Bankruptcy and Its Impact on Future Business Reorganizations*, 27 Emory Bankr. Dev. J. 25 (2010) (discussing possible interpretations of Supreme Court decision).
69. *See* Todd Zywicki, *The Rule of Law During Times of Economic Crisis*, *in* Economic and Political Change after Crisis: Prospects for Government, Liberty and the Rule of Law 36 (Stephen H. Balch & Benjamin Powell (eds), 2017).
70. Todd J. Zywicki, *Rent-Seeking, Crony Capitalism, and the Crony Constitution*, 23 S. Ct. Econ. Rev. 577 (2016).
71. *See* Jim Puzzanghera & Ken Bensinger, *GM, Chrysler Defend Slashing Dealerships*, Los Angeles Times (June 4, 2009), http://articles.latimes.com/2009/jun/04/business/fi-autos-congress4.
72. *See* Zywicki, *Auto Bailout*, *supra* note 1.
73. *See* James Sherk & Todd Zywicki, *Auto Bailout or UAW Bailout? Taxpayer Losses Came from Subsidizing Union Compensation*, Heritage Foundation Backgrounder No. 2700 (June 13, 2012).
74. Alex Nishimoto, *Rattner Says UAW Wages Should Have Been Cut During Bailouts*, Motortrend (Dec. 16, 2011), http://www.motortrend.com/news/rattner-says-uaw-wages-should-have-been-cut-during-bailouts-147425/.
75. Rattner, *supra* note 4, at 226.
76. *See* Special Inspector General for the Troubled Asset Relief Program, Treasury's Role in the Decision for GM to Provide Pension Payments to Delphi Employees (August 15, 2013).
77. *See* Zywicki, *Auto Bailout*, *supra* note 1 (listing examples).
78. *Id.*
79. *See* Todd J. Zywicki, *Chrysler and the Rule of Law*, Wall St. J., May 13, 2009, A19.
80. Lou Whiteman, *Buffett warns of Chrysler cramdown ramifications*, TheDeal.com (May 5, 2009) (quoted in Roe & Skeel, *supra* note 28, at 729).
81. Deniz Anginer & A. Joseph Warburton, *The Chrysler Effect: The Impact of Government Intervention on Borrowing Costs*, 40 J. Banking & Fin. 62 (2014).
82. Bradley Blaylock, Alexander Edwards & Jared Stanfield, *The Role of Government in the Labor-Creditor Relationship: Evidence from the Chrysler Bankruptcy*, 50(3) J. Fin. & Quantitative Analysis 325 (2015).
83. Rattner, *supra* note 4, at 44.
84. The following paragraphs are drawn from Zywicki, *Corporatist Legacy*, *supra* note 1.
85. *Id.* at 75.
86. *Id.*
87. *Id.*
88. *See* Benjamin Zhang, *The 20 Best-Selling Cars and Trucks in America*, Businessinsider.com (Jan. 7, 2017), http://www.businessinsider.com/best-selling-cars-trucks-vehicle-america-2016-2017-1/#20-hyundai-elantra-208319-sold-during-2016-down-138-over-2015-1.
89. The relevant others were Silverado (574,000) and RAM (489,000), leaving the Camry a distant fourth on the overall list at 388,000.
90. Jeff Cobb, *Chevy Bolt Sales Begin; Volt Smashes Sales Records*, www.hybridcars.com (Jan. 4, 2017), http://www.hybridcars.com/chevy-bolt-sales-begin-volt-smashes-sales-records/.
91. *See* Skeel, *supra* note 39, at 141.
92. *Id.*
93. *Id.*
94. *See* Todd J. Zywicki, *The Dodd-Frank Act Five Years Later: Are We More Stable?*, 43 J. Fin. Transformation 58 (2016).
95. Republican Staff of H. Comm. on Fin. Servs., 114th Cong., Unsafe at Any Bureaucracy: CFPB Junk Science and Indirect Auto Lending (2015).
96. Zywicki, *supra* note 94.

97. *In re* Motors Liquidation Co., 529 B.R. 510 (Bankr. S.D.N.Y. 2015).
98. *In re* Motors Liquidation Co., 829 F.3d 135 (2d Cir. 2016).
99. *Id.* at 160.
100. *Id.* at 165.