

Being so commonly thought of as a form of social welfare, it would surprise many people to know that bankruptcy developed as a legal right of creditors, not of debtors. In the first bankruptcies under English law, creditors would collectively force the liquidation of all a debtors' saleable property, distribute it accordingly, and be done with the matter. Modern bankruptcy law in the United States took a new step in the 1938 Chandler Act, which introduced a process of "reorganization" whereby debtors and small businesses could keep their property so long as they paid out more to creditors than would have been paid in a total liquidation. This was accomplished through a plan with regular payments to a trustee. Reorganization was ideal for economic efficiency, as it allowed debtors to continue earning money and contributing to the economy with the property they owned for their use, and paid debtors their due. However, both in the Chandler Act and afterward, such a simple reorganization was limited to lesser debtors. Corporations and those otherwise with severe debt were forced to file under a separate, more draconian chapter for reorganization.

Under the Chandler Act's provision for larger debtors, an effective reorganization of a corporation was nearly impossible. Unlike other reorganization provisions, it required a majority of similarly situated creditors to vote to confirm the plan. Likewise, the Act required an investigation by federal agents as to why the business was failing. Furthermore, under the Chandler Act, a trustee was required to take over the business, often one with little experience. Although some evidence suggests this was a mere formality and trustee let business managers continue operations, the Chandler Act was nonetheless virtually impossible to successfully reorganize under.

The flaws with the Chandler Act were recognized in the new United States Bankruptcy Code of 1978, which eliminated the investigation by government agents and allowed reorganizing businesses to ordinarily continue to run their own enterprises. While the approval of a majority of creditors was still a requirement, it was less problematic given the flexibility that a now unhindered reorganizing corporation had. But the new bankruptcy code was not without criticism. Some felt it was too lenient in the relief it gave to failing businesses to reorganize. Some question why businesses with large debts were able to file for bankruptcy at all as opposed to being merely liquidated.

The fact of the matter, however, is that time has demonstrated that it is more efficient to give business an attempt to reorganize and continue to contribute to the economy as oppose to be liquidated. Any remedy for creditors, whether bankruptcy or seizure of property by creditors, takes up the resources of government, which has an interest in resolving these debtor and creditor disputes in a manner most consistent with its policy goals.

6. Which one of the following most accurately expresses the main point of the passage?
- (A) Bankruptcy law in the United States was amended with the Chandler Act to include a provision for reorganization; however, this provision has proved of little use to reorganizing businesses and is seldom used today.
 - (B) Unlike most other developed nations, in the United States, large corporations can file reorganization bankruptcies to discharge their debt under a legal provision introduced in what was called the Chandler Act.
 - (C) The Chandler Act introduced a reorganization bankruptcy in the United States which, while flawed, was later refined, and then and now helped served the economic purposes of bankruptcy law.
 - (D) The first businesses to utilize the reorganization chapter of the Chandler Act in filing for bankruptcy were unsuccessful, and blamed their failures on problems with the act.
 - (E) The purpose of bankruptcy law is to encourage economic efficiency and maximize the economic output of past debtors, and this is accomplished through the modern provisions for bankruptcy reorganizations.
7. Based on the passage, which one of the following can be inferred about businesses which filed for reorganization under the discussed provision of the Chandler Act?
- (A) They were always corporations and not individuals.
 - (B) Their operations were taken over by a trustee.
 - (C) Without the Chandler Act, they invariably would have filed for the traditional liquidation bankruptcy.
 - (D) Most of them would have accomplished an effective reorganization under the reformed bankruptcy code of 1978.
 - (E) They always ceased business operations after the failure of an attempted reorganization under the Chandler Act.

8. The primary purpose of the third paragraph is to
- (A) illustrate how the strictness of the Chandler Act served to inhibit many business reorganizations
 - (B) compare problems with the Chandler act to contemporary problems in bankruptcy law
 - (C) give an example of the flaws elaborated upon in the second paragraph
 - (D) describe the process by which the government of the United States repealed the Chandler Act
 - (E) explain how the issues discussed in the second paragraph lead to a new development in the law.
9. The “mere formality” described in line 33 is most analogous to
- (A) a statue which is plated with silver so as to look as though it is solid silver when in fact it is made of clay
 - (B) a police officer who does not issue a citation for speeding even though the driver was in fact doing so
 - (C) a very young monarch who is nominally the sovereign of a nation but in fact invariably defers to the judgment of others
 - (D) a veterinarian whose practice is dedicated to treating cattle, but in fact treats many other types of animals
 - (E) a construction worker who always wears a helmet as a safety precaution, even on days when there could not possibly be danger
10. Which one of the following best describes the author’s attitude toward the Chandler Act’s reorganization provision for larger debtors that was described in the passage?
- (A) disgust in its shortcomings
 - (B) intrigue in its imperfect progress in bankruptcy law
 - (C) confidence in its longstanding effectiveness
 - (D) curiosity toward its individual debtor provisions
 - (E) indifference toward its effects since better legal remedies existed
11. According to the passage, each of the following was a requirement for businesses reorganizing under the discussed provision of the Chandler Act EXCEPT:
- (A) a plan which gave regular payments to a trustee
 - (B) an investigation by government agents concerning the failure of the business
 - (C) a confirmation vote by creditors of the business
 - (D) an option for the business to continue operations under its current management
 - (E) payment to creditors of a greater amount than they would have received in a liquidation
12. Based on the passage, which one of the following is true of bankruptcy as a legal action?
- (A) It was not often abused in the United States prior to 1978.
 - (B) It was originally a remedy for creditors, not debtors.
 - (C) It was not widely used by corporations before 1978.
 - (D) It was first adopted in the United States under the Chandler Act.
 - (E) It was not available to larger debtors before 1938.
13. Which one of the following examples provides the strongest support for the principle articulated in the fourth paragraph?
- (A) a shoe store badly damaged by a flood which over time would be able to pay significantly more, if not all, to its creditors than if its store were not immediately seized and sold to pay them
 - (B) a chain of software stores which has several unprofitable locations that need to be closed and liquidated so the remaining profitable stores can be maintained
 - (C) a freight hauling company which needs additional money and time to update and replace its truck fleet so that it can become profitable again
 - (D) an investment bank which, while generally profitable, has lost a great deal of money in a recent transaction and cannot repay a loan with the assets it has
 - (E) an apartment building which currently has a high rate of vacancy and is losing money, but will likely become profitable in a few years given the population growth in the particular area

GO ON TO THE NEXT PAGE