Revised Form of Rule 2019 Eliminates Purchase Price Disclosures by Committee Members

In chapter 11 bankruptcy cases, creditors and equity holders with common interests often find it advantageous to pool resources and form an ad hoc group or committee. Because the committee represents a larger amount of claims or interests, it speaks with more authority in the bankruptcy case, and the members are able to save money by sharing the cost of legal and financial advisors. In recent years, however, bankruptcy courts have enforced disclosure requirements under Federal Rule of Bankruptcy Procedure 2019 to require that ad hoc committee members publicly disclose the price paid for claims and interests purchased.

The Supreme Court recently approved a revised version of Rule 2019 that will lessen the future disclosure requirements for members of ad hoc committees. Assuming Congress does not block the amendment, it will automatically take effect on December 1, 2011 and will apply to all new and, "insofar as just and practicable," current cases.

The revised Rule 2019, like the current rule, will require the disclosure of the identity of each committee member and the amount of claims and interests such member holds. In a change from the prior rule, the new rule also requires the disclosure of other economic interests held by committee members, such as options to purchase claims or equity interests and derivatives related to claims or equity interests. The revised Rule 2019, unlike the current rule, also applies this requirement to official committees as of their formation date.

The revised rule resolves ambiguity under the current rule regarding which groups are required to comply with the rule. The current rule applies to a "committee" or an "entity" representing more than one creditor or interest holder. In recent years there has been substantial litigation over the meaning of the term "committee," with some courts interpreting it broadly to include ad hoc groups. Revised Rule 2019 codifies that view by expressly including within its ambit any group of unaffiliated creditors or interest holders acting in concert to advance their common interests.[1]

Revised Rule 2019 reverses one of the most controversial effects of the old rule by eliminating the requirement of disclosure of the purchase price paid by members for their positions. The current version of Rule 2019 requires each member of a committee to disclose when it acquired its claims or interests and the price it paid, except for claims or interests acquired prior to a year before the commencement of the case. Because this is highly sensitive, private commercial information for many creditors, the elimination of this requirement will be a welcome change.

The revised rule also limits the instances when ad hoc committee members must disclose the time of acquisition of securities. The current version of the rule requires each member to disclose when it acquired its claims and interests, unless they were acquired more than a year prior to the commencement of the bankruptcy case. The revised rule only requires a committee member to disclose time of acquisition if the

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1 Revised Rule 2019 includes exemptions for indenture trustees, agents for credit facilities, class action representatives, and governmental units, which would otherwise be captured by the broad language of the new rule.

committee represents an entity that is not actually a member of the committee. Further, even where disclosure is required, only the calendar quarter in which the claims or interests were acquired need be disclosed, not the precise date. As with the current version of the rule, no disclosure is required of the time of acquisition for claims or interests acquired more than a year before the bankruptcy case commenced.

As with the current rule, except for disclosures by members of official committees, the revised rule requires disclosure statements to be updated for "material" changes. The current rule requires such updates "promptly." The revised rule clarifies this by requiring an updated statement whenever an ad hoc committee takes a position in court or solicits votes on a plan.

The changes to Rule 2019 clarify its scope and eliminate the most commercially sensitive disclosures required by the current rule. These changes likely make participation on ad hoc committees more inviting for hedge funds, private equity funds, and other strategic claim purchasers.

If you would like to learn more about the changes to Rule 2019 and their impact on ad hoc committee service in bankruptcy cases, please contact your attorney at Ropes & Gray or any of the following:

Contact Information:

Mark Bane
212-841-8808
mark.bane@ropesgray.com

Alyson Allen
617-951-7483
alyson.allen@ropesgray.com