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# The Economics of Bankruptcy Reform

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We propose a new bankruptcy procedure. Initially, a firm's debts are cancelled, and cash and non-cash bids are solicited for the 'new' (all-equity) firm. Former claimants are given shares, or options to buy shares, in the new firm on the basis of absolute priority. Options are exercised once the bids are in. Finally, a shareholder vote is taken to select one of the bids. In essence, our procedure is a variant on the U.S. Chapter 7, in which non-cash bids are possible; this allows for reorganization. We believe our scheme is superior to Chapter 11 since it is simpler, quicker, market-based, avoids conflicts, and places appropriate discipline on management.

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