

# **FTX'd: Conflicting Public and Private Interests in Chapter 11**

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## **ABSTRACT**

Chapter 11 of the Bankruptcy Code is often justified by vague assertions that reorganizing troubled companies is in the “public interest.” There has, however, been surprisingly little effort to consider seriously what this public interest is, how it should be operationalized, or who should pay for it.

Based on a case study of the controversial bankruptcy of crypto complex FTX, this Article develops a three-part typology of public interests at stake in chapter 11 and shows how they can conflict with one another and with private interests: (1) The paramount public interest in the integrity of the judicial process; (2) bankruptcy-specific public interests in maximizing value through efficient, consolidated proceedings; and (3) “other” public interests, such as the prosecution and defense of serious crimes.

We place FTX’s counsel, Sullivan & Cromwell (S&C), at the center of this triptych. We present evidence which shows that S&C had undisclosed potential conflicts of interest due to apparent errors, omissions and deceptions in their work for the company and its founder, Sam Bankman-Fried, before, at and during the bankruptcy, thereby undermining the first-order public interest in procedural integrity. S&C’s role as debtor’s counsel has cast a troubling shadow over puzzling and costly decisions in the case, thereby undermining the second, bankruptcy-specific form of the public interest. S&C often justified its actions by reference to the third, “other” facet of the public interest, supporting the prosecution of disfavored insiders such as Bankman-Fried, a pricey task (they billed millions of dollars for this) which may have distorted those prosecutions without producing observable economic benefit to the bankruptcy estate.

FTX is a cautionary tale about the power that lawyers have to frame, control and profit from claims about the public interest in chapter 11. An examiner appointed late in the case largely exonerated S&C, although he engaged little of the evidence we present. This is not surprising because S&C’s resistance to that intervention left a narrow scope and little time for his investigation.

We situate our findings in a nascent body of literature exploring the public interest in bankruptcy and suggest that the experience with S&C in FTX may reflect larger patterns in reorganization reminiscent of

historical concerns about distorted incentives in restructuring processes. To ameliorate these concerns, we offer guidance to improve the functioning of the principal custodians of the public interest in chapter 11. Courts should more carefully police prebankruptcy connections by estate professionals and should use preliminary examinations more frequently. We further believe that the United States Trustee should have greater independence from other government actors so they can fulfill their watchdog mandate without compromise.