PART II

RECEIVERS AND REORGANIZERS

CHAPTER IX

CHOOSING THE RECEIVERSHIP JUDGE

CRAVATH, HENDERSON & DE GERSDORFF, the attorneys for the St. Paul bankers, explained to the Interstate Commerce Commission why they had drawn the receivership papers long in advance. They said that "no careful counsel would have postponed the preparation of these papers until after the board of directors had authorized, or some disgruntled creditor had precipitated, a receivership." Analysis of these words will disclose the gold in the ore. If the company required receivership, it would appear on the surface that there is no better reason for having the receivership papers drawn by the bankers' lawyers than by a real creditor, who still had his money invested in the property. There would seem to be more reason for the latter's doing it, since the bankers had sold their St. Paul bonds and were not creditors of the company at all. On the other hand, the way to correct a mistaken application by a creditor for the appointment of receivers would be to show the court that there was no justification for receivership, and not to have the bankers hurry to court with their own application for the appointment of receivers.

This helps to an understanding of what was really in the minds of the lawyers for the St. Paul bankers. Their concern was not with the state of mind of a creditor applying to a court to put the St. Paul into receivership. From their point of view, it would have been equally unsatisfactory whether the creditor

was disgruntled or happy. Their concern was that no creditor should apply for the appointment of receivers before the bankers themselves did so. The bankers wanted to be there first. Receivership is in one respect like a land rush in the days when the government opened new lands for settlement. All were waiting for the signal, to race at top speed for the choicest sections. There is, however, one difference between a land rush and a receivership rush. The first to arrive at the goal in the receivership race has, ordinarily, a rich opportunity to occupy all the land. His ability to realize on this opportunity is largely dependent upon his skill in selecting the judge who names the receivers of the property.

By selecting the judge who is most likely to appoint as receivers the men proposed by the bankers, the latter can place a railway in the hands of their own associates or friends. This, as will be later noted in detail, is of the greatest value. In addition, by having men sympathetic with themselves in an official relationship to the judge, considerable opportunity is afforded to produce a self-serving atmosphere. And on a number of matters, particularly in the earlier days of a receivership, before opposition has developed and when momentous decisions must be made, those who have been first in precipitating a receivership can have many of their desires satisfied without anyone else being present to oppose them.

Care in selecting the receivership judge is only one instance of a fairly common attitude on the part of lawyers who, like soldiers, know the value of a terrain favorable to themselves. If a lawyer can choose between different courts in which to try his case, and the decided law in one court is more promising to his client's interests than the law in another court, the lawyer goes to the first. So, in making his choice, he prefers the judge whose point of view seems most promising for his client. Where more than one judge holds court in a particular place, practicing lawyers know the care with which legal proceedings are nursed in such a manner as to get them before the judge of one's own heart. It would be asking too much to expect that equity re-

ceiverships, which provide the most lucrative field for such expressions of human nature, should be the outstanding exception to this practice, instead of being, as they are, the outstanding example.

The matter may be stated in the words of Paul D. Cravath, head of the law firm acting for the St. Paul company's bankers. He delivered some of the lectures prepared for the Association of the Bar of New York City on the subject of reorganizations. This was nine years before the St. Paul receivership. He advised promptness in going to court to get receivers appointed, in order to avoid "unfriendly receivership proceedings. The experienced reorganizer," he said, "stands in special dread of an unfriendly receivership proceeding. . . ."

The fear expressed by Mr. Cravath that someone else might apply for a receivership was no merely theoretical or imaginary one for his clients when the St. Paul affair came along some years later. In February a bondholder representing several million dollars' worth of the St. Paul bonds had tried to organize a committee and had called together the officials of several life-insurance companies which also had large holdings of the bonds. He had not invited the bankers to this meeting, but they learned of it from friends of theirs who were present. Here was a threat to the bankers' control of the situation. One of Mr. Hanauer's associates persuaded the independent bondholder to postpone further action. It was the latter's purpose to work out a voluntary readjustment, but if he changed his mind later and had a committee organized, receivership proceedings might be started before the bankers took that step. This would not only endanger, it might defeat, the opportunity which the bankers had in the spring of 1925 to intrench receivership and reorganization personnel of their own choosing.

Having decided to go forward with receivership, the bankers and their lawyers had to choose the judge for the purpose. They had considerable leeway. They might have selected a judge in Wisconsin, as the St. Paul company was a Wisconsin corporation and had railway mileage in that state. They might have gone to

states farther west, where the company had its lines of track also. It had a financial office and bank deposits and other property in New York. And in Chicago it had its principal operating office, as well as railway property. In some of these places, as for example in Chicago, the bankers' attorneys had a choice among several judges who conducted judicial business in the same court. On going to any such place the applicants for receivership could be sure that the judge selected by them would continue in charge of the receivership, even though judicial business is ordinarily rotated among the judges in such courts.

The decision of the bankers' attorneys was in favor of a receivership in Chicago. As one of the railway's lawyers said, "that business was done in Chicago." Among the judges in the Chicago district, Judge Wilkerson was chosen. He was consulted in advance, and for this purpose the bankers' attorneys employed their western representatives, Winston, Strawn & Shaw. This firm of lawyers was one of the most important in Chicago and in the country. At the time, various members of the firm were directors and counsel of a long list of large corporations, railway and industrial, and held or had held high public office, both in the federal government and elsewhere. If any firm had agreeable access to a federal judge in Chicago for an informal conference at which the important phases of a receivership might be arranged, it was this firm.

When Mr. Shaw, one of its partners, was being questioned in the Interstate Commerce Commission investigation about the March 15 meeting in Mr. Swaine's room, the following was said:

Mr. Prentice: Was there at that time any discussion as to the personnel of the receivers, or who should be requested?

Mr. Shaw: Yes, I think I was told that the people in the room had determined that they would ask in the first instance for the appointment of Mr. Byram and Mr. Potter.

It appeared much later in the investigation, from another witness, that the bankers had decided the question prior to the

Sunday meeting. Several days before Mr. Shaw had his Sunday meeting with the group of gentlemen, he had been requested over the long-distance telephone to carry out the bankers' decision, had promptly spoken to the Judge about it, and had made the arrangement for the appointment of Messrs. Byram and Potter. The facts were given by Mr. Miller, the company's New York attorney.

He said that at a conference between himself and the bankers' lawyers, on the subject of selecting Chicago lawyers for the proposed receivership, "it was agreed that Winston, Strawn & Shaw, by reason of their experience in such matters, would be suitable counsel for such a purpose. Mr. Shaw . . . was therefore communicated with by telephone by Mr. de Gersdorff and Mr. Swaine, of Cravath, Henderson & de Gersdorff [the bankers' lawyers] . . . and requested to ascertain whether Judge Wilkerson would be available on Wednesday, March 18, to receive and act upon a petition for a receivership should one be presented. Mr. Shaw was also requested to advise Judge Wilkerson as to the wishes of the company and the bankers as to the personnel of the receivers. Mr. Shaw reported that Judge Wilkerson would be available to act and that his disposition was to appoint Mr. Byram and Mr. Potter as receivers, as desired by the company and the bankers, with a third receiver selected personally by the court, and who would probably be E. J. Brundage, a former Attorney General of Illinois."

Mr. Potter, one of the receivers, when questioned by Mr. Grady, the attorney for the State of Wisconsin, in the Commission's investigation, said: "I know, and you know, and Ralph Shaw knows, and Mr. Miller [the company's New York lawyer] knows, that Judge Wilkerson never dickered with anybody about the appointment of a receiver, and never agreed to do anything, and never asserted any right, and nobody knows it better than you do."

The method chosen by the bankers' attorneys put them, of course, in a position in which they were, if not tacitly bargaining with the Judge, able to go shopping among the federal judges in

order to secure the appointment of the men they wanted as receivers. When Mr. Shaw interviewed Judge Wilkerson the week before any legal proceeding was brought, no papers were filed with the Judge or with the clerk of the court, and no legal action was formally instituted. If the Judge had indicated that he would not appoint the bankers' nominees, the bankers' attorneys could have interviewed another judge in Chicago, or a judge in some other city. The company's attorney was questioned on the point, as follows:

Mr. Grady: Do you mean to say that they said that they had had a conference with Judge Wilkerson before the appointment was made?

Mr. Miller: Yes.

Mr. Grady: As to whom he should select as receiver?

Mr. Miller: No. They had a conference with Judge Wilkerson telling him about this acute situation and asking him whether he would be available on the 18th day of March to hear a petition if it became necessary to file one. He said he would be ready. They discussed the importance of a railroad of this magnitude, and they said the company and the bankers would like to have Mr. Byram appointed as a receiver, and they would also like to have Mr. Potter as receiver, if agreeable to you; and as I got it, it is hearsay, of course, but as I got it, Judge Wilkerson said: 'Of course I do not know Mr. Potter, but Mr. Byram is perfectly satisfactory to me, and Mr. Potter is if you want him, but I want my own independent receiver, too'; and as I understand it, he said; 'My thought is that if it comes to a receivership that I do not know of any better man that I can appoint than Mr. Brundage.'"

Mr. Grady: Do you not consider that a most unusual procedure, to discuss a matter of that kind with a federal judge before filing the petition or invoking the jurisdiction of the court?

Mr. Miller: I do not wish to get into a discussion or argument with you on that. I can only say to you it is the usual precedent.

Mr. Shaw was asked to testify about his part in starting the receivership. This was several months before Mr. Miller went on the stand and told of Mr. Shaw's informal conference with Judge Wilkerson about a week in advance of the formal receivership proceeding. Mr. Shaw did not mention the informal conference and spoke only of what took place in Judge Wilkerson's chambers on March 18.

Mr. Shaw: We all met in his rooms at nine o'clock on Wednesday and presented the bill of complaint. . . .

Mr. Grady: Who were there?

Mr. Shaw: I was there; I think Judge Field was there—or Mr. Field, general counsel of the St. Paul road; and Judge Wilkerson was there; and I forget whether one of the bailiffs or one of the clerks was there in the room or not. I presented the bill, and told the story as I knew it.

Mr. Shaw also testified that one of his partners and one of the other attorneys of the railway company were present.

The forty thousand security-holders of the company, the investors who owned the property and whose property rights were to be fundamentally altered by the proceeding thus begun, were not represented before the Judge, either on March 18 or when Mr. Shaw was with him privately the week before. The directors had not been selected by the bondholders and could not claim to be their representatives. In so far as the proxies sent in by stockholders could be said to confer representative power on the board, it was for management of the business, and not for setting in motion a lawsuit to bring the company to an end.

Nor had the security-holders, the parties principally affected, received any notice of the intention to ask for Judge Wilkerson's order putting the property into receivership. Whether or not they could have been notified, the fact is that what took place before the Judge was in its essence a one-sided affair, at which lawyers carrying out the decision of the bankers had the only say, with most of the owners of the property absent and ignorant of what was being done.

Even some of the large owners who could easily have been notified were permitted to remain without prior notice of what was being done. The head of a concern which owned nine million dollars par amount of the junior bonds, probably the largest single holding of these bonds, had been led to believe that matters would remain quiescent for some time and was in the south at the time of the bankers' decision for receivership. Two days prior to the formal appearance on March 18 before Judge Wilkerson, this bondholder was requested by telegraph to become a member of a committee being organized by the bankers, but without any word that receivership was to be precipitated by them. If he had been told, there would still have been time for him to telegraph his attorneys to appear in court and speak on behalf of nine million dollars' worth of bonds. As it was, in his absence and in the absence of the other bondholders, lawyers not representing any bondholders, speaking in fact for bankers who had sold out well in advance and for directors most of whom represented no securities of the company, spoke their wishes to the Judge and had those wishes granted. Those wishes disposed of the property of others.

This one-sided proceeding, in which a handful of men induced a Judge to take action affecting a half billion of property values owned by persons from whom the affair had been kept secret, was of course a departure from the tried and approved methods of conducting ordinary judicial business in Anglo-Saxon countries. When one-sided proceedings of any sort are permitted, it is only in unusual circumstances. Even then it is usually required that those who obtain an order of the court shall submit evidence in sworn form, supporting their request, and that this evidence shall be filed in the court records so that absent persons who have been affected by the court's order may ascertain everything that goes on. In the St. Paul case the only sworn testimony was the complaint, which had been prepared in draft form by the bankers' lawyers in the preceding January. There was no evidence under oath showing the qualifications of the three men who were appointed receivers by the court order, or justifying

the grant to them of a dictatorship over a transcontinental railway.

Even the unsworn testimony on which the Judge acted was not made part of the court records. Apparently, there was not even a stenographer present to take down what was said, although what was said became the basis for court action affecting over forty thousand absent persons and hundreds of millions of dollars' worth of securities. Apparently the Judge signed the order of receivership just as it had been prepared by the bankers' lawyers in New York, with all the great powers which they sought to grant to their nominees.

One of the attorneys for the railway company and its receivers spoke, in the course of the Interstate Commerce Commission's investigation, of "the proper method to be adopted in the matter of these large corporate receiverships." He said that when the company's lawyer took part in the arrangements to put the St. Paul in receivership, he "participated in the adopting of that method which was recommended to the Bar Association as the correct procedure to follow in such cases."