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Proposed Counsel to the
Official Committee of Unsecured Creditors

50-275/323

**UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF CALIFORNIA
SAN FRANCISCO DIVISION**

In re:

PACIFIC GAS AND ELECTRIC
COMPANY, a California corporation,

Debtor.

Case No. SF 01-30923 DM

Chapter 11

**NOTICE OF MOTION AND MOTION
OF OFFICIAL COMMITTEE OF
UNSECURED CREDITORS FOR
ENTRY OF AN ORDER PERMITTING
TRADING IN AFFECTED SECURITIES
AND PUBLISHING RESEARCH UPON
ESTABLISHMENT OF ETHICAL
WALL PROCEDURES**

Hearing:
Date: [To Be Set]
Time: [To Be Set]
Place: 235 Pine Street, 22nd Floor
San Francisco, CA

[Motion For Order Shortening Time Filed
Concurrently]

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1 **TO THE HONORABLE DENNIS MONTALI, UNITED STATES BANKRUPTCY**
2 **JUDGE, ALL PARTIES IN INTEREST AND THEIR COUNSEL OF RECORD:**

3
4 **PLEASE TAKE NOTICE THAT** the Official Committee of Unsecured
5 Creditors (the "Committee") of Pacific Gas and Electric Company, the Debtor and Debtor in
6 Possession (the "Debtor") in the above-captioned chapter 11 case (the "Case"), hereby moves the
7 Court for entry of an order permitting members of the Committee to trade in the Debtor's
8 securities and debt, to trade in energy related commodities and derivatives, and to publish
9 research, all as more particularly described below, upon the establishment and implementation of
10 "Ethical Wall Procedures"¹ and in accordance with the terms and conditions of any such order
11 (the "Motion"). A hearing on this Motion has not yet been scheduled.

12 **I. RELIEF REQUESTED**

13 1. By this Motion, the Committee moves for the entry of an order,
14 substantially in the form of the proposed order attached hereto as Exhibit "1" (the "Proposed
15 Order"), determining that Committee members acting in any capacity will neither violate their
16 duties as Committee members nor subject their claims to possible disallowance, subordination or
17 other adverse treatment by buying, selling or otherwise trading in, or in publishing research
18 relating to, any of the following during the pendency of the Debtor's chapter 11 case,

- 19 (i) the Debtor's stock, notes, bonds, debentures, and commercial paper or other
20 paper,
21 (ii) participations in any of the Debtor's debt obligations,

22
23
24 ¹ As used herein, the term "Ethical Wall Procedures" refers to procedures established by an
25 institution to isolate its trading activities from its activities as a member of an official creditors'
26 committee. An Ethical Wall Procedure typically involves: staffing arrangements whereby the
27 institution's personnel responsible for performing committee functions are different from the
28 personnel responsible for performing trading and research functions; physical separation of the
office and file spaces used by those personnel; establishment of procedures for securing
committee-related files; establishment of separate telephone and facsimile lines for trading
activities and committee activities; and special procedures for the delivery and posting of
telephone messages.

1 (iii) credit derivatives, gas, power, coal, and other commodities, including without
2 limitation physical, financial, derivative and other transactions and products,
3 involving or relating to the Debtor or its affiliates, or in the markets in which the
4 Debtor or its affiliates conduct the same or similar operations or in other markets,
5 or
6 (iv) any other claims against or interests in the Debtor, ((i) and (ii) and (iv)
7 collectively, the "Affected Securities" and (iii) the "Affected Commodities") as long as any
8 Committee member that engages in any such transactions in Affected Securities or Affected
9 Commodities establishes and effectively implements policies and procedures to prevent the
10 misuse of any non-public information that may be obtained through its activities as a Committee
11 member ("Confidential Committee Information").

12 II. FACTS

13 A. BACKGROUND

14 2. On April 6, 2001, the Debtor filed a voluntary petition for relief under
15 chapter 11 of title 11 of the United States Code (the "Bankruptcy Code"). The Debtor is
16 operating its business and managing its property as debtor in possession pursuant to Bankruptcy
17 Code sections 1107(a) and 1108.

18 3. On April 10, 2001, the United States Trustee appointed the Committee,
19 and on April 13 and 20, 2001, the United States amended its appointments to the Committee. As
20 of the date hereof, the Committee consists of the following eleven (11) members: Bank of
21 America, NA, PE-Berkeley, Inc., The Bank of New York, City of Palo Alto, The Davey Tree
22 Surgery Company, Dynegy Power Marketing, Inc., Enron Corp., GWF Power Systems, LP, State
23 of Tennessee, Merrill Lynch and Morgan Guaranty. In addition, the Committee has selected
24 Bank of America, NA and PE-Berkeley, Inc. to serve as Co-Chairs of the Committee.

25 4. On April 16, 2001, the Committee selected Milbank, Tweed, Hadley &
26 McCloy LLP ("Milbank") as counsel to represent the Committee in the Case. Milbank has
27 separately filed an application for employment for this Court's approval.
28

1 5. This Court has jurisdiction over this Motion pursuant to 28 U.S.C. §§ 157
2 and 1334 and this matter is a core proceeding under 28 U.S.C. § 157(b)(2). The statutory
3 predicate for the relief sought by this Motion is Bankruptcy Code section 105(a).

4 **B. NEED FOR REQUESTED RELIEF**

5 6. Certain members of the Committee, and certain direct or indirect affiliates
6 or subsidiaries of members of the Committee, among other functions, trade in, or render financial
7 advice (including providing research) with respect to the Affected Securities or the Affected
8 Commodities, including but not limited to municipal, public and private securities, and energy
9 related commodities and derivatives, as a regular part of their business (collectively, the
10 “Trading Entities”).

11 7. The Trading Entities are among the largest creditors of the Debtor and
12 bring considerable expertise to the Committee. Therefore, the Trading Entities have both the
13 incentive and ability to make significant contributions to the Committee and this Case.

14 8. However, the Trading Entities are unwilling to serve on the Committee if
15 they are not permitted, pursuant to reasonable Ethical Wall Procedures, to trade in, and/or, as the
16 case may be, render financial (including providing research) advice with respect to, the Affected
17 Securities and the Affected Commodities, which include, but are not limited to, those Affected
18 Securities or Affected Commodities held by the Trading Entities as of the date hereof or
19 subsequently directly or indirectly acquired by them.

20 9. As members of the Committee, Trading Entities may receive information
21 regarding the Debtor that has not been released to the public and which may be released only
22 subject to a confidentiality agreement. Absent entry of the Proposed Order, the Trading Entities
23 may not be authorized to trade in the Affected Securities or the Affected Commodities, or
24 publish research relating thereto, without being accused of violating their fiduciary duties as
25 Committee members, thus subjecting their claims in this case to possible disallowance or
26 subordination, or subjecting themselves or their clients to disgorgement of trading profits or
27 other adverse treatment.

28

1 10. Many institutions have faced the same dilemma in other chapter 11 cases
2 in recent years. To resolve this issue, bankruptcy courts, with increasing regularity, permit
3 institutional creditors and broker/dealers to trade in the securities of a debtor while serving on an
4 official creditors' committee. Such authorization, however, typically is conditioned on such
5 institutional creditors establishing Ethical Wall Procedures.

6 11. The use of Ethical Wall Procedures will protect the public from any harm
7 that might otherwise occur by virtue of a Trading Entity's simultaneous service on or to the
8 Committee and continued trading in the Affected Securities and the Affected Commodities and
9 publication of research. At the same time, entry of the Proposed Order will benefit the public by
10 allowing the significant market players that sit on the Committee to actively trade, which will
11 assist in providing liquidity for the Affected Securities and the Affected Commodities.

12 **III. ARGUMENT**

13 **A. AUTHORIZING TRADING AND RENDERING ADVICE WITH**
14 **RESPECT TO AFFECTED SECURITIES AND AFFECTED**
15 **COMMODITIES BY COMMITTEE MEMBERS IS IN THE BEST**
16 **INTERESTS OF THE ESTATE AND THE MARKET**

17 12. Procedures for establishing an Ethical Wall were clearly articulated by the
18 United States Bankruptcy Court for the Southern District of Ohio in the chapter 11 bankruptcy
19 case of Federated Department Stores, Inc. 1991 WL 79143, Bankr. No. 1-90-00130, (Bankr.
20 S.D. Ohio 1991). In that case, Fidelity Management & Research Company ("Fidelity"), a
21 member of an official bondholders' committee, moved for an order determining that it would not
22 violate its duties as a committee member by trading in the debtor's securities if procedures were
23 implemented to insulate its trading activities from its committee-related activities. Numerous
24 parties, including the Securities and Exchange Commission (the "SEC"), supported Fidelity's
25 motion, and even the debtor responded that they were not opposed to the requested relief. The
26 SEC's memorandum, attached hereto as Exhibit "2," in support of Fidelity's motion urged the
27 court to adopt the SEC's position that:

28 consistent with the requirements of the federal securities laws and the bankruptcy
 laws, an entity that is engaged in the trading of securities as a regular part of its

1 business and that has implemented procedures reasonably designed to prevent the
2 transmission to its trading personnel of information obtained through service on
3 an official committee *is not precluded from serving on the committee and, at the*
4 *same time, trading in the debtor's securities.*

5 SEC Memorandum at 6 (emphasis added). The SEC went on to point out that institutional
6 creditors "have skills and expertise that are likely to be extremely valuable to the committee" and
7 concluded that there "is no legal impediment to permitting the service of such entities on official
8 committees." Id.

9 13. Fidelity's motion was granted, with Judge Aug ordering that "Fidelity will
10 not be violating its fiduciary duties as a committee member and, accordingly, will not be
11 subjecting its claims to possible disallowance, subordination, or other adverse treatment by
12 trading in the securities of the Debtor . . . during the pendency of these Cases, provided that
13 Fidelity employs an appropriate information blocking device or [Ethical] Wall." In re Federated
14 Dep't Stores, Inc., 1991 WL 79143 at *1 (the "Federated Order").

15 14. The Federated Order specified certain procedures for establishment of an
16 Ethical Wall by an institutional creditor, including: (i) written acknowledgment by personnel
17 performing committee work that they could receive non-public information and are aware of the
18 Ethical Wall Procedures in effect; (ii) preventing the trading entity's trading personnel from the
19 misuse of any non-public information obtained by the trading entity's designated representatives
20 for Committee-related activities; (iii) creation of separate file space for committee work that is
21 inaccessible to employees that are not responsible for performing any committee-related
22 functions; (iv) restrictions on committee personnel's access to trading information; and (v)
23 establishment of a compliance review process.

24 15. Since the entry of the Federated Order, numerous other bankruptcy courts,
25 including the United States Bankruptcy Court for the Central District of California, have
26 recognized the importance of having institutional creditors participate on official committees in
27 large cases, and accordingly, have entered orders permitting institutional members of official
28 committees to trade the debtor's securities and publish research as long as Ethical Wall
Procedures are implemented.

1 16. For example, in In re County of Orange, Case No. SA 94-22272-JR, Judge
2 Ryan entered an order (January 31, 1995), a copy of which is attached hereto as Exhibit "3,"
3 permitting members of the official committee of unsecured creditors and the subcommittee of
4 bondholders to trade in the debtor's, and other, securities with "appropriate and effective
5 information blocking procedures," the terms of which were substantially identical to those set
6 forth in the Federated Order.

7 17. More recently, by orders dated October 19, 2000, December 11, 1999,
8 September 21, 1999, December 21, 1998, February 21, 1997, July 17, 1996 and September 8,
9 1995, in the respective chapter 11 cases of In re GST Telecom, Inc., Case No. 00-1982 (GMS),
10 In re Sun Healthcare Group, Inc., Case No. 99-3657 (MFW), In re ICO Global Communications
11 Services Inc., et. al., Case No. 99-2933 (MFW), In re Acme Metals Inc., Case No. 98-2179
12 (MFW), In re Mid American Waste Systems, Inc., Case No. 97-104 (PJW), In re Ace-Texas,
13 Inc., et al., Case No. 96-166 (PJW), and Wherehouse Entertainment, Inc., Case No. 95-911
14 (HSB), the Bankruptcy Court for the District of Delaware has permitted members of the official
15 creditors' committees appointed in such cases to trade in the debtors' securities during the
16 pendency of such cases provided that the committee members established and implemented
17 Ethical Wall Procedures. Other bankruptcy courts have entered similar orders. See In re Vista
18 Eyecare, Inc., Case No. A00-65214 (Bankr. D. Ga. June 1, 2001); In re America West Airlines,
19 Inc., No. 91-07505 (Bankr. D. Ariz. Oct. 23, 1991).

20 **B. USE OF "INFORMATION WALLS" IS PERMITTED**
21 **UNDER SECURITIES LAWS AND REGULATIONS**
22 **AND NOT PRECLUDED UNDER THE BANKRUPTCY CODE**

23 18. As noted in the SEC Memorandum, "[Ethical] Walls and similar devices
24 are well-established means of preventing transmission of [material nonpublic] information . . ."
25 Id. at pg. A-162. Moreover, such devices are mandated for broker-dealers and investment
26 advisers. 15 U.S.C. § 780(f) and 15 U.S.C. § 80b-4A.²

27 _____
28 ² Both sections (one from the Securities Exchange Act and the other from the Investment
Advisers Act of 1940) provide for the establishment, maintenance and enforcement of written

1 19. Under certain circumstances, Ethical Wall Procedures may provide
2 defenses to asserted violations of Rule 14e-3 of the Securities Exchange Act of 1934 (“Rule 14e-
3 3”). Rule 14e-3 mandates a “disclose or abstain from trading duty” for any person who obtains
4 inside information about a tender offer from either the offeror or the target company, or from
5 their officers, directors or employees. An exception to the Rule exists for those entities that can
6 show the individuals making the investment decisions are not privy to the inside information and
7 that the entity has implemented policies and procedures, reasonable under the circumstances, the
8 ensure that the securities laws would not be violated. Rule 14e-3(b).

9 20. The SEC, in the SEC Memorandum, argues that the same legal principles
10 provided for in Rule 14e-3(b) should extend to Section 10(b) of the Securities Exchange Act and
11 Rule 10b-5 thereunder.³ See Koppers v. American Express, 689 F. Supp. 1413, 1413-5 (W.D.
12 Pa. 1988) (reprinting letter to court from the Commission’s General Counsel stating that the
13 Commission “believes that violations of the federal securities laws stemming from these
14 conflicts can be avoided through the use of well-established preventative policies and
15 procedures, such as [Ethical] Walls, restricted lists and watch lists.”); Slade v. Shearson,
16 Hammill & Co., Inc., Fed. Sec. L. Rep. (CCH) ¶ 94, 329 (S.D.N.Y. 1974), remanded 517 F.2d
17 398 (2d Cir. 1974) (supporting the use of Ethical Wall Procedures in brokerage firms if the
18 persons who engage in securities transactions for customers are thereby effectively isolated from
19 any inside information that the firm may receive as an investment banker).

20 21. While it is clearly established that members of official committees are
21 fiduciaries to the creditors they represent,⁴ no current Bankruptcy Code provision prevents the
22 trading in claims or securities of the Debtor or the publication of research relating thereto.
23 Indeed, when Congress enacted the Bankruptcy Code in 1978, it specifically deleted section 249

24 *cont'd . . .*
25 policies and procedures reasonably designed to prevent the misuse of material, nonpublic
26 information.

26 ³ Under Section 10(b) and Rule 10b-5 thereunder, an insider having material, nonpublic
27 information must disclose the information or abstain from trading in order to avoid violating
28 those provisions.

28 ⁴ See Woods v. National Bank and Trust Co. of Chicago, 312 U.S. 262, 268-69 (1941).

1 of the former Bankruptcy Act, which provided that fiduciaries would be denied compensation for
2 services rendered in the bankruptcy proceedings if they engaged in any trading in the debtor's
3 securities.

4 22. Bankruptcy Code section 328(c), the successor to section 249 of the
5 Bankruptcy Act, authorizes the denial of compensation to professionals who are not
6 disinterested, but unlike section 249 of the Bankruptcy Act it does not apply to members of an
7 official or unofficial committee nor is it a mandatory denial of compensation. 11 U.S.C.
8 § 328(c).

9 23. The SEC interpreted the omissions of the prohibitions cited in section 249
10 of the Bankruptcy Act as the intent of Congress to "give more flexibility for interpretation of the
11 fiduciary duty that is owed by members of official committees." SEC Memorandum at page 22.
12 This Court should extend that flexibility to permit Trading Entities to trade in, provide research
13 coverage of, and render advice with regards to Affected Securities and Affected Commodities, as
14 long as they comply with the established procedural protections set forth in the Proposed Order.

15 **C. COMMITTEE MEMBERS SHOULD NOT BE**
16 **PRECLUDED FROM TRADING, PROVIDING RESEARCH COVERAGE**
17 **OF, OR RENDERING ADVICE WITH RESPECT TO, THE AFFECTED**
18 **SECURITIES AND THE AFFECTED COMMODITIES**

19 24. The Committee believes that current and future members of the
20 Committee should not be precluded from trading in, providing research coverage of, or rendering
21 advice with respect to, Affected Securities and Affected Commodities during the tenure of such
22 member(s) on the Committee. As recognized by the SEC in the Federated case, the Trading
23 Entities have resources and experience, including knowledge of the Debtor's business, industry,
24 capital structure and the gas and power markets, that render them particularly valuable for
25 official creditors' committee service. In addition, because the Trading Entities are among the
26 Debtor's largest creditors (or representatives thereof), they have a great incentive to pursue the
27 Committee's work diligently toward the goal of confirming a chapter 11 plan.

28 25. Beyond any negative consequences it would have in this case, denial of
the relief sought herein also will discourage large creditors with expertise and experience in

1 reorganizations from joining creditors' committees in other cases, despite the presumption in the
2 Bankruptcy Code that the committee will "ordinarily" consist of the largest creditors. See 11
3 U.S.C. § 1102(b)(1). Creditors that regularly trade in the Debtor's securities or in commodities
4 also traded by the Debtor simply should not be forced into the choice of serving on a committee
5 and risking the loss of beneficial investment opportunities or business opportunities or
6 transactions for their clients or foregoing service and possibly compromising those same
7 responsibilities by taking a less active role in the reorganization.

8 26. Accordingly, the Committee seeks entry of the Proposed Order which
9 provides a mechanism for the authorized trading of the Affected Securities and the Affected
10 Commodities by the Trading Entities. Many courts have entered similar orders to permit
11 Committee members to trade in and provide research with respect to the debtor's securities,
12 provided Ethical Wall Procedures were implemented. There is no impediment in the federal
13 securities laws, other laws or the Bankruptcy Code to the relief sought by the Committee.
14 Indeed, for some time now, the SEC has recognized the value and legitimacy of Ethical Wall
15 Procedures in the securities law context. As bankruptcy courts have repeatedly recognized, there
16 is no reason why Ethical Wall Procedures cannot prove to be just as useful in the bankruptcy
17 context.

18 27. For the foregoing reasons, the Committee respectfully submits that its
19 members should be permitted to trade in, and provide research with respect to, the Affected
20 Securities and the Affected Commodities during the pendency of this case on the condition that
21 such members establish and effectively implement policies and procedures, such as the Ethical
22 Wall Procedures, to prevent the misuse of non-public information obtained through their
23 activities as Committee members.

24 **IV. NOTICE**

25 28. Notice of this Motion has been given to the Office of United States
26 Trustee, the Securities and Exchange Commission, the New York Stock Exchange, the National
27 Association of Securities Dealers, the Commodities Futures Trading Commission, the Chicago
28

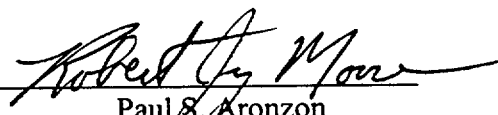
1 Board of Trade, members of the Committee, and counsel to the Debtor. The Committee submits
2 that due to the nature of the relief requested herein, no further notice is required.

3 V. CONCLUSION

4 **WHEREFORE**, the Committee respectfully requests the entry of an order,
5 substantially in the form of the Proposed Order annexed hereto as Exhibit "1," providing that a
6 Committee member acting in any capacity will not violate its duties as a Committee member
7 (and, accordingly, will not subject its claims to possible disallowance, subordination, or other
8 adverse treatment) by publishing research and trading in Affected Securities or Affected
9 Commodities during the pendency of the Debtor's cases, provided that such Committee member
10 implements the applicable Ethical Wall Procedures to insulate its research and trading activities
11 from the activities related to its Committee service; and (ii) grants the Committee such further
12 relief as the Court deems just and appropriate.

13
14 Dated: May 16, 2001

MILBANK, TWEED, HADLEY & M^cCLOY LLP

15
16 By: 
17 Paul S. Aronzon
Robert Jay Moore

18 Proposed Counsel to the Official Committee of Unsecured
19 Creditors of Pacific Gas and Electric Company
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Of Pacific Gas and Electric Company

6

7

8

**UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF CALIFORNIA
SAN FRANCISCO DIVISION**

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In re:

Case No. 01-30923-DM

12

**PACIFIC GAS AND ELECTRIC
COMPANY**, a California corporation,

Chapter 11

13

Debtor.

**[proposed] ORDER PERMITTING
TRADING IN AND PUBLISHING
RESEARCH WITH RESPECT TO
AFFECTED SECURITIES UPON
ESTABLISHMENT OF ETHICAL
WALL PROCEDURES**

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Federal I.D. No. 94-0742640

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Hearing:

19

Date: [To Be Set]

20

Time: [To Be Set]

21

Place: 235 Pine Street, 22nd Floor
San Francisco, CA

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[Motion For Order Shortening Time Filed
Concurrently]

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Upon the motion (the "Motion") of the Official Committee of Unsecured
Creditors (the "Committee") of Pacific Gas and Electric Company (the "Debtor") for an order
permitting members of the Committee to publish research and trade in the Affected Securities
and the Affected Commodities (as defined in the Motion) upon establishment of certain "ethical

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PROPOSED ORDER APPROVING TRADING MOTION

1 wall" procedures (the "Ethical Wall Procedures"), and due and proper notice of the Motion
2 having been given, and after due deliberation, and sufficient cause appearing therefor, it is
3 hereby found and

4 ORDERED, that any Committee member acting in any capacity will not be
5 violating its fiduciary duties as a Committee member and, accordingly, will not subject its claims
6 to possible disallowance, subordination, or other adverse treatment, if any such Committee
7 member and/or its affiliates publishes research and/or trades in the Debtor's Affected Securities
8 and/or in the Affected Commodities during the pendency of this case (the "Trading Entity"),
9 provided that such Trading Entity establishes and maintains Ethical Wall Procedures to prevent:
10 (i) the employees of such Trading Entity engaged in preparing and publishing research and/or in
11 effecting or consummating trades on a day to day basis in the Affected Securities or the Affected
12 Commodities or employees to whom such trading employees directly report (collectively,
13 "Trading/Research Personnel") from misusing any non-public information obtained by such
14 Trading Entity's designated representative(s) for Committee-related activities ("Committee
15 Personnel"); and (ii) Committee Personnel from receiving information regarding (a) such
16 Trading Entity's trading in the Affected Securities or the Affected Commodities in advance of
17 such trades, or (b) the content of such Trading Entity's research relating to the Affected
18 Securities in advance of the publication of such research; and it is further

19 ORDERED, that the Ethical Wall Procedures to be employed by a Trading Entity,
20 if it wishes to trade in the Affected Securities and/or the Affected Commodities, and/or to
21 prepare and provide research relating thereto shall be deemed adequate procedures if they
22 include the following information-blocking procedures (it being understood that some of the
23 Trading Entities have established internal procedures regarding ethical walls devised from
24 longstanding compliance with federal and state securities laws and regulations): (i) Committee
25 Personnel will share non-public Committee information ("Confidential Committee Information")
26 only with employees of such Trading Entity that, due to such employee's duties and
27 responsibilities, have a need to know such information (including, without limitation, senior
28 management with direct and indirect oversight responsibility over the work or activities of the

1 Committee Personnel with respect to their participation as the Trading Entity's representative(s)
2 on the Committee, employees providing assistance to the Committee Personnel with respect to
3 their participation as the Trading Entity's representative(s) on the Committee, and regulatory and
4 compliance personnel, auditors and in-house legal personnel for the purpose of rendering
5 regulatory, compliance audit or legal advice); (ii) notwithstanding the foregoing, Committee
6 Personnel and any other persons described in subsection (i) that receive Confidential Committee
7 Information will not share such information with any of such Trading Entity's Trading/Research
8 Personnel unless otherwise approved by in-house counsel; (iii) the Trading Entity shall notify in
9 writing all Committee Personnel and either (a) such other employees that are reasonably likely to
10 receive Confidential Committee Information; or (b) any other person approved by in-house
11 counsel who subsequently receives Confidential Committee Information, that during the
12 pendency of the Case (as defined in the Motion) they may receive Confidential Committee
13 Information, of the existence of this Order, and of their responsibility to comply with the Ethical
14 Wall Procedures that are in effect with respect to the Affected Securities and the Affected
15 Commodities; (iv) Committee Personnel and all other persons receiving Confidential Committee
16 Information shall keep such information in files that are inaccessible to Trading/Research
17 Personnel; (v) Committee Personnel will receive no information regarding the Trading Entity's
18 trades in the Affected Securities or the Affected Commodities in advance of such trades, nor the
19 content of any research related to the Affected Securities in advance of the publication of such
20 research, except that Committee Personnel may receive:

- 21 (a) the usual and customary internal and public reports showing the Trading
22 Entity's purchases and sales and the amount and class of securities and the
23 amount and types of commodities and derivatives owned by such Trading
24 Entity, including the Affected Securities and the Affected Commodities, and
25 copies of research reports issued by such Trading Entity after such reports are
26 released to the public, and
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(b) information regarding the Trading Entity's trades or proposed trades in the Affected Commodities with the Debtor or its affiliates in advance of such trades.

In the event that Committee Personnel inadvertently receive such information, no violation of this Order shall be deemed to have occurred if Committee Personnel promptly disclose the receipt of such information to the Committee and abstain from voting on any matter which might be affected by such information; and (vi) the Trading Entity's compliance department personnel shall review from time to time the Ethical Wall Procedures employed by the Trading Entity as necessary to ensure compliance with this Order and shall keep and maintain records of their review; provided, however, that this Order is not intended to preclude the Court from taking any action it may deem appropriate in the event that it is determined that an actual breach of fiduciary duty has occurred because the procedures employed have not been effective or for reasons unrelated to the relief granted in this Order; and it is further

ORDERED, that the provisions of this Order shall automatically apply and inure to the benefit of all present Committee members, as well as any entities that become members of the Committee after the date hereof.

Dated: May __, 2001

HONORABLE DENNIS MONTALI
UNITED STATES BANKRUPTCY JUDGE

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FAX NO. 212 351 4035

P. 16

UNITED STATES BANKRUPTCY COURT
FOR THE SOUTHERN DISTRICT OF OHIO
WESTERN DIVISION

No. 1-96-00120

In re:

FEDERATED DEPARTMENT STORES, INC.
and
ALLIED STORES CORPORATION, et. al.,
Debtors.

MEMORANDUM OF THE SECURITIES AND EXCHANGE COMMISSION
IN SUPPORT OF MOTION OF FIDELITY MANAGEMENT & RESEARCH CO.

JAMES R. DOTY
General Counsel

JACOB H. STILLMAN
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THOMAS L. RIESENBERG
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Securities and Exchange Commission
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of Counsel
PAUL GONSON
Solicitor

APR-09-2001 MON 03:22 PM GDC

FAX NO. 212 351 4035

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3. Trading should be permitted only by entities which are engaged in the trading of securities as a regular part of their business 23

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as committee members. entitles would constitute a breach of their fiduciary obligations their trading in the securities of the debtor and the related 11 bankruptcy proceeding has stated to members of the committee on the committee. The United States Trustee in Allied's Chapter provide a means of nonpublic information obtained through review preventive procedures, such as Chinese Walls, are implemented to federated bankruptcy proceedings as long as appropriate Allied and its affiliates during the pendency of the Allied and duties as a committee member in the securities of of the court determining that fidelity will not be violated in Allied Stores Corporation ("Allied"). Fidelity requests an order at the Official Bankruptcy Committee (the "committee") of Fidelity Management & Research Co. ("Fidelity") as a member

MEMORANDUM OF THE SECURITIES AND EXCHANGE COMMISSION AND STAFF OF ITS POSITION

MEMORANDUM OF THE SECURITIES AND EXCHANGE COMMISSION

Debtors:

ALLIED STORES CORPORATION, ET AL.,
 AND
 REDEEMED EXCHANGE STORES, INC.

IN RE:

NO. 1-90-0710

UNITED STATES BANKRUPTCY COURT
 FOR THE SOUTHERN DISTRICT OF OHIO,
 WESTERN DIVISION

The securities and exchange commission, which acts as an advisor to the court in bankruptcy reorganization cases pursuant to section 1103(a) of the bankruptcy code, 11 U.S.C. 1103(a), suggests this procedure because it believes that the procedure being urged by the U.S. trustee would deprive the creditors of the benefits of the expertise of the committee that the commission would encourage with respect to financial institutions and other entities that trade securities as a regular part of their business from relying on their committees. Since such entities have a substantial financial interest in the outcome of the bankruptcy proceeding and can thus be expected to devote significant time and resources to the effort concerned, activities, such as a audit would be contrary to the best interests of public investors.

As the court, the commission believes it is important to assess that person who serves on official committees should be viewed as "temporary trustees" like Bank v. SEC, 463 U.S. 866, 867 n. 14 (1983), and are subject to the provisions against alleged insider trading that are applicable to other such trustees. In addition, it should be noted that entities which serve as such temporary trustees, like fidelity in this case, have found that it is good corporate practice to establish appropriate preventive procedures, such as Chinese walls, as a means of preventing misuse of nonpublic information and of avoiding liability under the federal securities laws. The

Commission has in recent years encouraged this development. As to the more specific question presented in this case, the Commission believes that, consistent with the requirements of the federal securities laws and the bankruptcy laws, an entity which is engaged in the trading of securities as a regular part of its business and which has established procedures reasonably designed to prevent the transmission to its trading personnel of information obtained through review on an official committee is not precluded from trading on the committee and, at the same time, trading in the debt or a security. Includes such as investment advisers, broker-dealers, pension funds, banks, or insurance companies have, in some cases bankruptcy, been among the larger creditors. Such institutions have existed and expected that are likely to be especially valuable to the committee. There is no legal impediment to permitting the review of such entities on official committees.

EXPLANATION OF THE CASE

Committee to bankruptcy proceedings for Allied and its estate, Federated Department Stores, Inc. ("Federated"), are pending before this court. Allied owns 50% of Federated Holdings, Inc., which wholly owns Federated. In addition, Allied's parent, Federated Stores, Inc., directly or indirectly owns all of the stock of Ralph's Grocery Stores, Inc. ("Ralph's"). Approximately 16.3% of Ralph's stock is owned directly by Allied. Allied, Federated and Ralph's are all issuers of publicly traded "junk" bonds. As part of the

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reorganization proceedings, official committees for both Allied and Federated were appointed.

On March 5, 1990, the U.S. Trustee sent a letter to an official Federated bondholders' committee stating that members of that committee are precluded from trading in the securities of Federated or its affiliates. In his letter, the U.S. Trustee stated that "continued trading in the securities of the Debtors and their related entities would constitute a breach of your fiduciary obligations as committee members. . . . The above trading restrictions shall be in effect until the date a plan of reorganization has been formally approved by the Court, and regardless as to whether your service on the committee has been terminated, [sic] earlier." The members of the Allied Committee have been informed by the U.S. Trustee that, in his view, the same trading prohibitions would apply to them.

On January 3, 1991, Fidelity moved that this Court enter an order determining that Fidelity will not be violating its duties as a committee member by trading in the securities of Allied, Federated or Ralph's.

DISCUSSION

- A. Persons who serve on official committees should be viewed as "temporary insiders" of the debtor who are subject to the insider trading prohibitions of the federal securities laws that are applicable to other such insiders.

Under Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder, an insider having material, nonpublic information about his company must disclose the information or

operate from trading in order to avoid violating those

provisions. See *SEC v. Texas Gulf Sulphur Co.*, 401 F.2d 812 (2d Cir. 1968) (en banc), cert. denied, 394 U.S. 378 (1969); *Shelton v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 493 F.2d 228 (2d Cir. 1974). In the bankruptcy context, the interest of an

official committee is properly viewed as "resortly interest," *Dixie*, 623 F.2d at 655, n. 14; that is, persons who, like an underwriter, accountant, lawyer, or consultant working for the corporation, "have entered into a special confidential

relationship in the conduct of the business of the enterprise and are given access to information solely for corporate purposes." If such persons are subject to the same insider trading

restrictions as are insiders such as corporate officers, see *SEC v. Gornblatt*, 751 F.2d 1024, 1027-28 (2d Cir. 1984), *State*, 104 S. Ct. 316 (1991); *SEC v. Johnson*, 684 F. Supp. 1457, 1459-60 (C.D. Cal. 1988); *SEC v. Morse*, 618 F. Supp. 596, 616-17 (S.D.N.Y. 1986), *State*, 633 F.2d 1096 (2d Cir. 1981), cert. denied, 458 S. Ct. 1251 (1982). Thus, official committee members who trade

while in possession of material information about the debtor operating and relying on the committee violate the anti-insider provisions of the federal securities laws.

It is good corporate practice for entities which serve an official committee to establish appropriate preventive procedures, such as Chinese walls, in order to protect against issues of material, nonpublic information and because the existence of such protective device may enable them to avoid violating the anti-insider provisions.

A focus of protecting against the misuse of material,

nonpublic information obtained by entities to ensure that such

information is not transmitted to persons within the entity who

are responsible for making trading decisions, unless walls and

existing devices are well-established means of preventing the

transmission of such information, and if the good corporate

practice for entities which serve on official committees to

establish Chinese walls and similar procedures in order to

protect against the abuse of information. Such devices have the

practical and prophylactic effect of preventing information from

being disseminated within entities except on a "need to know"

basis. 1/

In addition, under the Index dealing securities fund

Investment Act of 1980 (ITSEA), such devices are mandated for

broker-dealers and investment advisers. Section 15(c) of the

Securities Exchange Act, 15 U.S.C. § 78n(c), and § 204 of the

Investment Advisers Act of 1940, 15 U.S.C. § 80b-4, which were

added by ITSEA, provide that every registered broker or dealer

and every investment adviser subject to § 204 of the Investment

Advisers Act must establish, maintain, and enforce written

policy and procedures reasonably designed, taking into account

the nature of the business involved, to prevent the misuse of

material, nonpublic information.

1/ See, e.g., In re Merrill Lynch, Pierce, Fenner & Smith, Inc., 43 S.E.2d 523 (1968). See generally, Lavin, Galtman, and Evanson, "Nonpublic Securities Law and the Federal Securities Act," 53 Harv. L. Rev. 281, 312-16 (1981).

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Chinese Walls and other preventive procedures may also provide a defense to actions brought under the antifraud provisions. The particular characteristics of that defense, and their application to this situation, are discussed in the following section.

C. Consistent with the requirements of the federal securities laws and the bankruptcy laws, an entity which is engaged in the trading of securities as a regular part of its business and which has established procedures reasonably designed to prevent the transmission of information obtained through service on an official committee is not precluded from serving on the committee and, at the same time, trading in the debtor's securities.

1. The federal securities laws should not preclude trading.

We would agree with the U.S. Trustee's position in this case if members of the Allied Committee would violate the federal securities laws by trading in Allied securities while simultaneously serving on the Committee. We believe, however, that, through establishment of preventive procedures such as a Chinese Wall, entities that engage in the trading of securities as a regular part of their business can serve on official committees and simultaneously trade without violating the antifraud provisions.

An entity, by engaging in multiple activities, may subject itself to insider trading liability in several different situations. In the classic case, the investment banking department of a firm may acquire material, nonpublic information about a company at the same time that the broker-dealer department of the firm is recommending or executing customer

Transactions in the securities of that company first on public

information that is inconsistent with the confidential

information data by the investment banking department. In this

situation, the firm must reconcile the duty to the investment

banking client with the duty to the retail customer. As an

agent of the investment banking client, the firm has the duty to

preserve the confidentiality of the client, nonpublic

information that is acquired through the investment banking

relationship. As the firm does, however, the firm is

providing services for the retail customer, and, at least when

it makes such recommendations, must reveal any material, adverse

information it possesses to those customers. As a branch of that

duty is applicable, under the so-called "shingle theory," the

violation of Rule 10b-5. See, e.g., *Smith v. SEC*, 115 F.3d 539

(2d Cir. 1997).

Chinese Wall and related devices may provide a defense to

2/ See RESTATMENT (SECOND) OF AGENCY § 305 (1998); UNIFAC

principled not to use or communicate information

confidentially given him by the principal or acquired by him

during the course of or on account of the agency; . . .

that obligation continues even after the formal agency

relationship between the parties ends. See RESTATMENT

(SECOND) OF AGENCY, § 306(d). See also LAUREN, UNIFORM

SECURITIES ACT, COMMENTARIES TO § 17(b), UNIFORM

SECURITIES ACT, COMMENTARIES TO § 17(b), UNIFORM

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SECURITIES ACT, COMMENTARIES TO § 17(b), UNIFORM

(continued...)

(2) Such person had implemented one or more activities of political and propaganda, reasonable under the circumstances, taking into consideration the nature of the person's business, to ensure that individual(s) making investments would not violate

(1) The individual(s) making the investment decision on behalf of such person to purchase or sell any security determined in paragraph (a) as to cause any such security to be purchased or sold by or on behalf of others and not for the benefit, nonpublic information; and

A person other than a natural person shall not violate paragraph (a) of this section if such person shows that:

Rule 10b-3(b) states:

that the securities law would not be violated. If and procedures, reasonable under the circumstances, to ensure inside information and that the entity has implemented policies individuals making the investment decision are not privy to the exception from this duty for entities that can show that the the actual nature of nonpublic information, the rule provides an directs of employee. Since the rule's objective is to prevent other the extent of the target company, or even their officers, person who obtains inside information about a tender offer issue which mandates a disclosure or abstain from trading duty for any under rule 10b-3. In 1980, the Commission adopted Rule 10b-3, has prohibited the use of Chinese walls as a defense to liability the liabilities arising from these conflicts. The Commission

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Although the Commission has not codified the use of preventive procedures as a means to avoid securities law liability except in Rule 14e-3, the same legal principles extend to actions under Section 10(b) of the Securities Exchange Act and Rule 10b-5 thereunder. See Statement of David S. Ruder, Chairman, Securities and Exchange Commission, before the Subcommittee on Securities of the Senate Banking, Housing and Urban Affairs Committee, Concerning the Commission's Revised Proposal to Define Insider Trading (Dec. 15, 1987); Letter from Chairman John S.R. Shad to Honorable Timothy E. Wirth (June 25, 1983), reprinted in H.R. Rep. No. 355, 98th Cong., 1st Sess. 28 (1983). See also Koppers v. American Express, 559 F. Supp. 1413, 413-15 (W.D. Pa. 1988) (reprinting letter to the court from the Commission's General Counsel stating that the Commission "believes that violations of the federal securities laws stemming from these conflicts can be avoided through the use of well-established preventive policies and procedures, such as Chinese

4/ (...continued)

paragraph (2), which policies and procedures may include, but are not limited to, (i) those which restrict any purchase, sale and causing any purchase and sale of any such security or (ii) those which prevent such individual(s) from knowing such information.

See Securities Act Release No. 6239, Fed. Sec. L. Rep. (CCH) ¶ 22,646 at B3,461 (Sept. 4, 1980).

HAIR, registered trademark and service mark of the

A Chinese Hall defense is available for trademark holders in
also provided under section 212(a) of the Securities
Exchange Act, which was added by H.R. 1774, provides for the
imposition of civil penalties on persons who control a person
who engages in illegal insider trading. Section 212(b)(1) (A),
however, provides that in order to speak such penalties the
Commission must show that at least one of the conditions stated
one of these is that the controlling person "knowingly or
recklessly failed to establish, maintain, or enforce any policy
or procedure required under section 212(c) of the Exchange Act
in section 204 of the Investment Advisers Act of 1940 and
such failure substantially contributed to or resulted in the

See also cited by the Commission in Shady v. Shady,
Hampshire Co., Inc., Fed. Sec. L. Rep. (CCH) ¶ 64,325
(S.D.N.Y., 1974), amended 517 F.2d 298 (2d Cir., 1974)
(supporting the use of Chinese Hall's trademark for
the persons who engage in securities transactions for
customers are thereby effectively isolated from any inside
information that the firm may receive as to investment
markets) and Doyle and Govers, Chinese Hall's trademark
of a good business practice, 36 Am. Bus. L. Rev. 155 (1988)
(advocating Chinese Hall practices as good business
practice for investment firms and specifically elements of an
effective Chinese Hall) and Lee Leung, Hui, Hui, Hui
regulates firms' trading with conflicts in a tender offer
context, 33 Wake Forest L. Rev. 43-58 (1998) (citing that
although there are no cases directly addressing the issue,
the SEC likely views an effective Chinese Hall as a
defense for a registrant firm in an action charging the
firm with insider trading violations of Rule 10b-5 or Rule
14e-3).

See Shady p. 8.

The alternative data for obtaining civil penalties from a controlling person is, under Section 21(a)(1)(A), that the controlling person knew or recklessly disregarded the fact that such controlling person was likely to engage in the act of acts constituting the violation and failed to take appropriate steps to prevent such act or acts before they occurred.

In the Commission's view, persons who should be expanded to include this category, as in the other categories, there exists a strong policy rationale in favor of allowing certain financial institutions to trade while acting on official committees, entities such as investment advisers, brokerage firms, banks, pension funds, or insurance companies.

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have, in some recent bankruptcies, been among the largest creditors. Such institutions have skills and expertise that are likely to be useful to the committee. In addition, as the largest creditors of the debtor, they are likely to devote substantial time and resources to the official committee's activities.

1. The bankruptcy laws should also not preclude trading.

2. The former Bankruptcy Act

(1) Section 249

As to the bankruptcy laws, it is well established that members of official committees are fiduciaries to the creditors they represent. 1/ Section 249 of the former Bankruptcy Act provided that fiduciaries would be denied compensation for services rendered in the bankruptcy proceeding if they engaged in any trading in the debtor's securities. 2/ The provision related

1/ See Hoads v. City National Bank and Trust Co. of Chicago, 112 U.S. 362, 384-89 (1901); In re Continental Investment Corp., 617 F. 2d 8, 10 (1st Cir. 1980); In re Conservator, Wash. Coal Corp., 156 F. 2d 3, 5 (3d Cir. 1947), cert. denied, 110 U.S. 777; In re Midland United Co., 61 F. Supp. 399, 417 (D. Del. 1948); In re Central States Electric Corp., 112 F. Supp. 281, 287 (D. Va. 1953), cert. denied sub nom Kenis v. Scan, 146 U.S. 899.

2/ Section 249 provided:

Any persons seeking compensation for services rendered or reimbursement for costs and expenses incurred in a proceeding under this chapter shall file with the court a statement under oath showing the claims against, or stock of, the debtor, if any, in which a beneficial interest, direct or indirect, has been acquired or transferred by him or for his account, after the commencement of such

(continued...)

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would frustrate the anti-fraud intent of Congress to impose an effective prophylactic rule." 372 U.S. at 855. 11/

There is, however, no case law discussing the ramifications of Chinese Walls or any other type of preventive procedure under Section 249 or in this context generally. In one case a court implicitly accepted the concept of a Chinese Wall when it allowed compensation under Section 249 to an attorney to a defendant shareholders' committee. In re Philadelphia Reading Coal &

Iron Co., 61 F. Supp. 129 (E.D. Pa. 1945). The attorney's wife

11/

There are cases in which Section 249 was not interpreted so broadly. For instance, in In re Midland United Company, 64 F. Supp. 399 (D. Del. 1946), the court allowed compensation to members of an official committee who belonged to brokerage houses that dealt to a small extent in the securities of the debtor's subsidiaries and affiliates. The court stated that in general a fiduciary dealing in such securities should not be compensated under Section 249 because the fiduciary would place himself in a position of conflict. For instance, he might be able to impede the reorganization of the debtor by foreclosing on the assets of the subsidiaries. The court noted that in this case the trading was for the benefit of the fiduciaries' husbands, not for the fiduciaries' own account, and the fiduciaries did not inspire the trading. Id. at 415-17. In essence, the court seemed to suggest that the financial remuneration that the brokerage firms would receive from trading in the securities of the debtor's subsidiaries and affiliates on behalf of other parties would not be sufficient to establish a conflicting interest. In another decision, In re Central State Electric Corporation, 112 F. Supp. 281 (E.D. Va. 1953), the court concluded that the attorneys for a bankruptcy reorganization committee that represented the debtor's shareholders were not precluded by Section 249 from receiving compensation even though they directly or indirectly through their families, traded in the securities of the debtor's subsidiaries. In reaching this conclusion, the court interpreted Section 249 as granting the court discretion to require compensation with respect to subsidiaries. It allowed compensation in this case because neither the reorganized shareholders nor the debtor's estate had been prejudiced by the transactions. Id. at 287.

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had traded in the securities of the debtor during the reorganization. The issue was raised as to whether the attorney should be denied compensation because trading by the wife was arguably the same as trading by the husband. The court concluded that because the attorney had never apprised his wife of any inside information obtained from the committee and was unaware of his wife's purchases, he should not be denied compensation. 16. at 128. The court seemed implicitly to conclude that a satisfactory *de facto* Chinese Wall had been implemented to insulate the wife from inside information.

(2) Section 212

An additional provision of the former Act, Section 212, also has some bearing on this issue. It reflected the general principle that fiduciaries should not profit because of their position. Under this section, the courts had the discretionary power to review the circumstances surrounding a fiduciary's acquisition of claims or securities, and to limit the fiduciary's recovery to the amounts paid for such claims or securities. 12/

12/ Section 212 provided:

The judge may examine and disregard any provision of a deposit agreement, proxy, power or warrant of attorney, trust mortgage, trust indenture, or deed of trust, or committee or other authorization, by the terms of which an agent, attorney, indenture trustee, or committee purports to represent any creditor or stockholder, may enforce an accounting thereunder, may restrain the exercise of any power which he finds to be unfair or not consistent with public policy, and may limit any claim or stock acquired by such person or committee in contemplation or in the course of the proceeding

(continued...)

12/ (...continued)
under this chapter to the actual consideration
paid thereon.
(Emphasis added.)
See in re Continental Investment Corp., 527 F.2d 8, 11 (5th Cir., 1975).

Even if there had been case law under sections 213 and 214 calling for the precise question raised here — that is, the use of Chinese walls to provide an exception to a prohibition on creating by committee entities — we do not believe that such case law would be directly applicable today, since neither section was

b. The present statutory code
Even if there had been case law under sections 213 and 214 calling for the precise question raised here — that is, the use of Chinese walls to provide an exception to a prohibition on creating by committee entities — we do not believe that such case law would be directly applicable today, since neither section was

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carried over into the current bankruptcy code. The legislative history on this matter is unclear as to Congress' intent, but nothing suggests that Congress intended the result urged by the U. S. Justice in this case.

The Senate bill that was first proposed incorporated Section 249 into a new proposed Section 330(b). In that section, however, was omitted from the final bill that became the bankruptcy code. Very little explanation was given for this omission other than a statement by Senator DeConcini that the section was "deleted as unnecessary, as the limitations contained

11/ Proposed Section 330(b) stated:

No compensation or reimbursement shall be allowed to any committee, attorney, or other person acting in a representative or fiduciary capacity who, at any time after assuming to act in such capacity, has purchased or sold claims of stock, or by whom or for whose account such claims or stock have, without the prior consent or subsequent approval of the court, been otherwise acquired or transferred.

The Senate Report discussing Section 330(b) made clear that, in the Senate's view, Section 249 prohibited committee members from trading in the debtor's securities. It stated:

Subsection (b) repeats section 249 of Chapter X of the bankruptcy Act (11 U.S.C. 649). It is a codification of equitable principles designed to prevent fiduciaries in the case from engaging in the specified transactions since they are in a position to gain inside information or to shape or influence the course of the reorganization. (Citation omitted.) The statutory bar of compensation and reimbursement is based on the principle that such transactions involve conflicts of interest. . . .

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therein are covered by section 328(c) of E.R. 3200." 15/
 However, an analysis of Section 328(c) of the new code indicates
 that Section 328(c) differs in certain respects from Section 249.
 Section 328(c) 16/ authorizes denial of compensation to
 professionals who are not disinterested, but unlike section 249,
 it does not apply to members of official or unofficial
 committees. Also, while Section 249 absolutely prohibited
 compensation if the person traded in claims or equity securities
 of the debtor, Section 328(c) is discretionary with the court.

One possible -- and the most likely -- explanation for the
 omission of the prohibitions cited in Section 249 is that
 Congress intended to give more flexibility for interpretation of
 the fiduciary duty that is owed by members of official
 committees. In general, the bankruptcy court is not constrained
 by statute, but can look to its general equitable powers to
 restrict fiduciary trading. See, e.g., American Mutual Life
 Insurance Co. v. City of Avon Park, 311 U.S. 138, 146 (1940) (a

15/ 124. Congressional Record S. 17406 (Oct. 6, 1978).

16/ Section 328(c) provides:

Except as provided in section 327(c), 327(e),
 or 327(b) of this title, the court may deny
 allowance of compensation for services and
 reimbursement of expenses of a professional
 person employed under section 327 or 329 of
 this title if, at any time during such
 professional person's employment under
 section 327 or 329 of this title, such
 professional person is not a disinterested
 person, or represents or holds an interest
 adverse to the interest of the estate with
 respect to the matter on which such
 professional person is employed.

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bankruptcy courts' powers are "not dependent on express statutory provisions"). In light of the recognized equitable powers of bankruptcy courts and the Code's silence regarding the fiduciary duties of official committee members, it is arguable that Congress intended to allow a less restrictive interpretation of fiduciary duties under the new Code. The legislative history of the current Code also suggests that, in drafting the Code, Congress may have taken into consideration the sophistication of the bankruptcy bar today, as well as recent developments in the securities laws. For instance, in the House Report on the bill that was ultimately enacted as the current Code, there is a discussion about why the proposed bill made the appointment of a trustee in a Chapter 11 reorganization case discretionary. The Report states: "Reorganization law and practice has changed substantially in the past 40 years, however, and the absolute necessity for a trustee in every case has ceased. The serious abuses of the 1930's have largely been cured by the adoption of the securities laws, and their vigorous enforcement by the Securities and Exchange Commission." H.R. Rep. No. 595, 95th Cong., 2nd Sess. 233, reprinted in 1978 U.S. Code Cong. & Ad. News 5565, 6192 (1978).

3. Trading should be permitted only by entities which are engaged in the trading of securities as a regular part of their business.

The Commission does not urge that the Court hold that all entities be permitted to trade in the securities of the debtor while serving on an official committee. Chinese Walls are not

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deal-probes, and therefore an absolute bar to trading would be a more effective means of preventing the misuse of material, nonpublic information. Also, there are arguments rooted in bankruptcy law that no trading should be allowed by committee members. The Commission therefore believes that trading by committee members should only be permitted if there exists a significant policy rationale in favor of allowing trading. A "Chinese Wall exception" should only be available to firms that engage in the trading of securities in their regular course of business. Such entities -- such as investment advisers, investment banking firms, brokerage firms, pension funds, and insurance companies -- have the type of expertise which is valuable to official committees.

In addition, such entities traditionally have considerable experience with the implementation of Chinese Walls. See, e.g., Securities Act Release No. 5239, 20 SEC Dkt. 1241, 1252 (Sept. 4, 1980) (in promulgating Rule 144-3, the Commission stated that it "understands that policies and procedures to prevent the use of material, nonpublic information relating to a tender offer as well as other types of information are widely used by multi-service financial institutions."). See also Broker-Dealer Policies and Procedures Designed to Segment the Flow and Prevent the Misuse of Material Nonpublic Information, [1989-90 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 64,529 (March 1990). Moreover, it is unfair to force such an entity to make a choice between serving on a committee and continuing to engage in its regular

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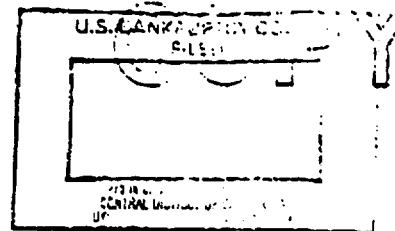
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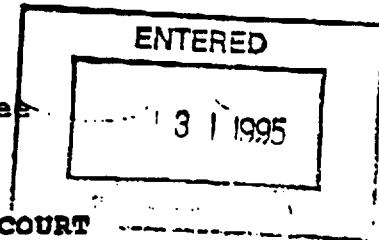
business; such a dilemma is not faced by entities which do not regularly engage in securities trading.

As a final point, the Commission urges this Court to require the entity to file a copy of its Chinese Wall or other preventive policies and procedures with the bankruptcy court prior to trading. Such written notice would likely serve as a deterrent to illegal insider trading and would require that the entity take its obligations in this area seriously. 17/

17/ We note that we are merely urging a filing requirement; we are not suggesting that the bankruptcy court review the adequacy of the Chinese Wall procedures.



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6 Proposed Attorneys for the Official Committee
 of Creditors of the County of Orange

8 UNITED STATES BANKRUPTCY COURT

9 CENTRAL DISTRICT OF CALIFORNIA

10

11	In re	)	Case No. SA 94-22272-JR
12		)	(Administratively Consolidated with
13	COUNTY OF ORANGE, a	)	Case No. SA-94-22273-JR)
14	political subdivision of	)	Chapter 9
15	the State of California;	)	(This Pleading Applies to Case No.
16	ORANGE COUNTY INVESTMENT	)	SA-94-22272-JR only)
17	POOLS, an instrumentality	)	ORDER GRANTING MOTION OF THE OFFICIAL
18	of the County of Orange,	)	COMMITTEE OF UNSECURED CREDITORS OF
19		)	THE COUNTY OF ORANGE FOR ORDER
20	Debtors.	)	REGARDING TRADING OF MUNICIPAL
21		)	SECURITIES BY MEMBERS OF OFFICIAL
22		)	COMMITTEE AND OFFICIAL SUBCOMMITTEES
		)	Date: January 31, 1995
		)	Time: 11:00 a.m.
		)	Place: Courtroom 606
		)	34 Civic Center Plaza
		)	Santa Ana, CA 92701

23 AT SANTA ANA, CALIFORNIA, IN SAID DISTRICT, THIS 31st
 24 DAY OF January, 1995:

25 The Court, having read and considered the "Motion of the
 26 Official Committee of Unsecured Creditors of the County of Orange
 27 For Order Regarding Trading of Municipal Securities by Members of
 28 Official Committees and Official Subcommittees" (the "Motion") and

1 the Declaration of Richard Kuersteiner in Support Thereof (the
2 "Kuersteiner Declaration"), and the responses of the County of
3 Orange and the Securities and Exchange Commission thereto, based
4 upon the pleadings, exhibits and documents of record in this case,
5 and having determined notice of the Motion was proper and other
6 good cause appearing therefor, it is hereby

7 ORDERED, that

8 1. The Motion is granted in its entirety;

9 2. For purposes of this Order, the term "Trading
10 Entities" shall mean all present or future members or ex officio
11 members of the Committee, the Official Subcommittee of Bondholders
12 (the "Subcommittee"), advisors to the Committee and the
13 Subcommittee, and/or the direct or indirect affiliates of any of
14 them, which are multi-service financial institutions which, among
15 other functions, trade in, or render financial advice with respect
16 to, municipal securities as a regular part of their business;

17 3. Trading Entities will not be violating any
18 fiduciary duties as members or ex officio members of or advisors
19 to the Committee or the Subcommittee, and accordingly will not be
20 subjecting their claims to possible disallowance, subordination,
21 disgorgement of trading profits or other adverse treatment, by
22 trading in or rendering financial advice with respect to
23 securities of the County and OCIP Participants, provided that the
24 Trading Entities comply with the provisions of paragraph 4, below;

25 4. Each Trading Entity shall either: (a) refrain from
26 trading any Affected Securities issued by the Debtor or any OCIP
27 Participant at any time that the Trading Entity is in possession
28 of nonpublic information regarding the Debtor (whether or not such

1 information might be subject to public disclosure in the event of
2 a proper request under one or more Public Access Laws); or
3 (b) institute appropriate and effective information blocking
4 procedures which prevent specified employees of Trading Entities,
5 including investment professionals advising on and securities
6 traders engaged in trading of Affected Securities, from receiving
7 any such nonpublic information provided to the Committee, the
8 Subcommittee or the advisors and to prevent the representatives of
9 the Trading Entity sitting on or advising the Committee or the
10 Subcommittee from receiving information regarding the Trading
11 Entity's trading in Affected Securities, which procedure shall be
12 served on counsel for the County and the Committee, the Office of
13 the United States Trustee and the Securities and Exchange
14 Commission. Trading Entity personnel who are in possession of
15 Committee Information will not receive any information regarding
16 trades in Affected Securities more frequently than every ten days.
17 Trading Entities relying on clause (a) above shall maintain
18 records regarding the dates on which, and reasons why, trading has
19 been suspended pursuant to clause (a) and identifying trading
20 personnel involved in Committee business and the reasons for such
21 involvement. Such records shall be served promptly following such
22 suspension or involvement on counsel to the County and the Commit-
23 tee, and the Office of the United States Trustee and the Securi-
24 ties and Exchange Commission. Without limiting the generality of
25 clause (b) above, it shall constitute full compliance with such
26 clause (b) if the Trading Entity institutes and complies with the
27 following "information wall" procedures: (i) the Trading Entity
28 shall have all personnel who have access to nonpublic information

1 arising out of their functions as members of or advisors to the
2 Committee ("Committee Information") execute a letter acknowledging
3 that they may choose to receive nonpublic information and that
4 they are aware of the "information wall"; (ii) Trading Entity per-
5 sonnel will not share nonpublic Committee Information with any
6 affiliated personnel who may trade in or render financial advice
7 with respect to, Affected Securities; and (iii) compliance profes-
8 sionals of the Trading Entity shall review all trades in Affected
9 Securities to confirm that such trades were made in conformity
10 with the procedures set forth in this order and shall keep records
11 of such reviews or such Trading Entity shall otherwise direct its
12 compliance professionals to effectuate the foregoing provisions of
13 this paragraph with respect to all trading in Affected Securities;
14 provided, however, that this Order is not intended to preclude the
15 Court from taking any action it deems appropriate in the event
16 that it is determined that an actual breach of fiduciary duty has
17 occurred because the procedures employed are not so effective or
18 for reasons unrelated to the fact of any Trading Entity's ability
19 to trade based on the establishment of the procedures set forth
20 herein; and

21 5. This Order shall inure to the benefit of all
22 present and future members or ex officio members or advisors to
23 the Committee or to the Subcommittee who are Trading Entities
24 intending to engage in trading of Affected Securities.


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28

JOHN E. RYAN
HONORABLE JOHN E. RYAN
UNITED STATES BANKRUPTCY JUDGE

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Presented by:

MURPHY, WEIR & BUTLER

By: 
Mary L. Young
Proposed Attorneys for
the Official Committee of
Unsecured Creditors

1 PROOF OF SERVICE

2 STATE OF CALIFORNIA, COUNTY OF LOS ANGELES

3 I am employed in the County of Los Angeles, State of California. I am over the age of 18
4 and not a party to the within action; my business address is 601 South Figueroa Street, 30th
Floor, Los Angeles, California 90017.

5 On May 17, 2001, I served the foregoing document(s) described as NOTICE OF
6 MOTION AND MOTION OF OFFICIAL COMMITTEE OF UNSECURED CREDITORS FOR
7 ENTRY OF AN ORDER PERMITTING TRADING IN AFFECTED SECURITIES AND
PUBLISHING RESEARCH UPON ESTABLISHMENT OF ETHICAL WALL PROCEDURES
on the interested parties in this action:

8 By placing the true copies thereof enclosed in sealed envelopes addressed as stated on
the attached mailing list.

9 By placing the original a true copy thereof enclosed in sealed envelopes
10 addressed as follows:

11 SEE ATTACHED SERVICE LIST

12 (BY MAIL)

13 I deposited such envelope(s) in the mail at Los Angeles, California. The envelope(s)
were mailed with postage thereon fully prepaid.

14 Following ordinary business practices at the Los Angeles, California office of Milbank,
15 Tweed, Hadley & McCloy LLP, I placed the sealed envelope(s) for collection and mailing
with the United States Postal Service on that same day. I am readily familiar with the
16 firm's practice for collection and processing of correspondence for mailing. Under that
practice, such correspondence would be deposited with the United States Postal Service
17 on that same day, with postage thereon fully prepared at Los Angeles, California, in the
ordinary course of business.

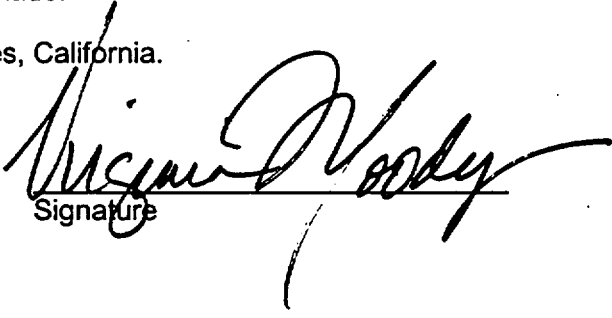
18 (BY OVERNIGHT COURIER) I caused the document to be delivered, in an envelope
19 with postage prepaid, to be sent by Federal Express.

20 (BY FAX) I caused all of the pages of the above-entitled document to be sent to the
recipients noted via electronic transfer (FAX) at the respective telephone numbers
21 indicated.

22 (FEDERAL) I declare that I am employed in the office of a member of the bar of this
23 court at whose direction the service was made.

24 Executed on May 17, 2001, at Los Angeles, California.

25 Virginia Moody
26 Type or Print Name

Signature 

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141 West Jackson Boulevard
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15 SEE ATTACHED SERVICE LIST

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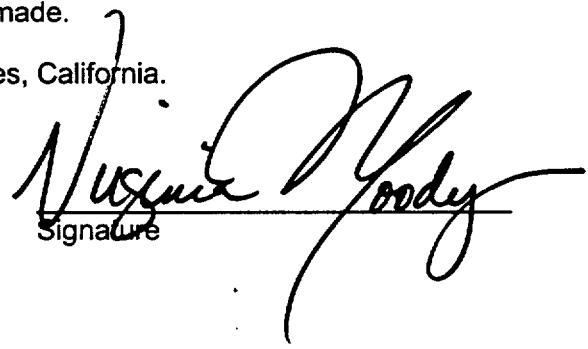
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28 Executed on May 23, 2001, at Los Angeles, California.

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