
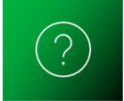







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Welcome and Some Housekeeping Items

	Be sure to sign-in for MCLE Credit at the registration desk.
	Ask questions! Our panelists are happy to engage with you.
	If your attendance time meets the rules set by the Illinois MCLE Board, ACC Chicago will send your certificate by email next week.
	Watch for the survey/feedback link sent to your email after the program.

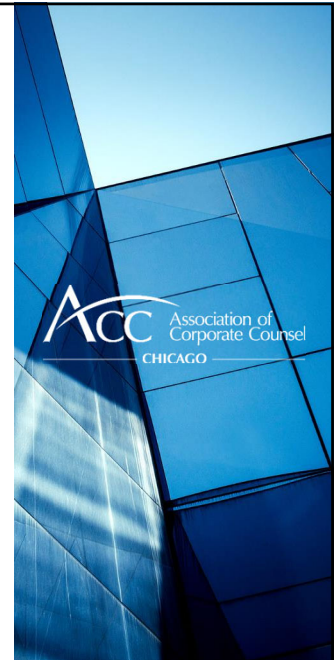
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A Reminder About the Benefits of ACC Membership

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- Access to ACC Global Resources, including:
 - ACC Docket Magazine & Newsstand (searchable legal news feed)
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 - E-Groups and Committees on Substantive Practice Areas




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Presenters



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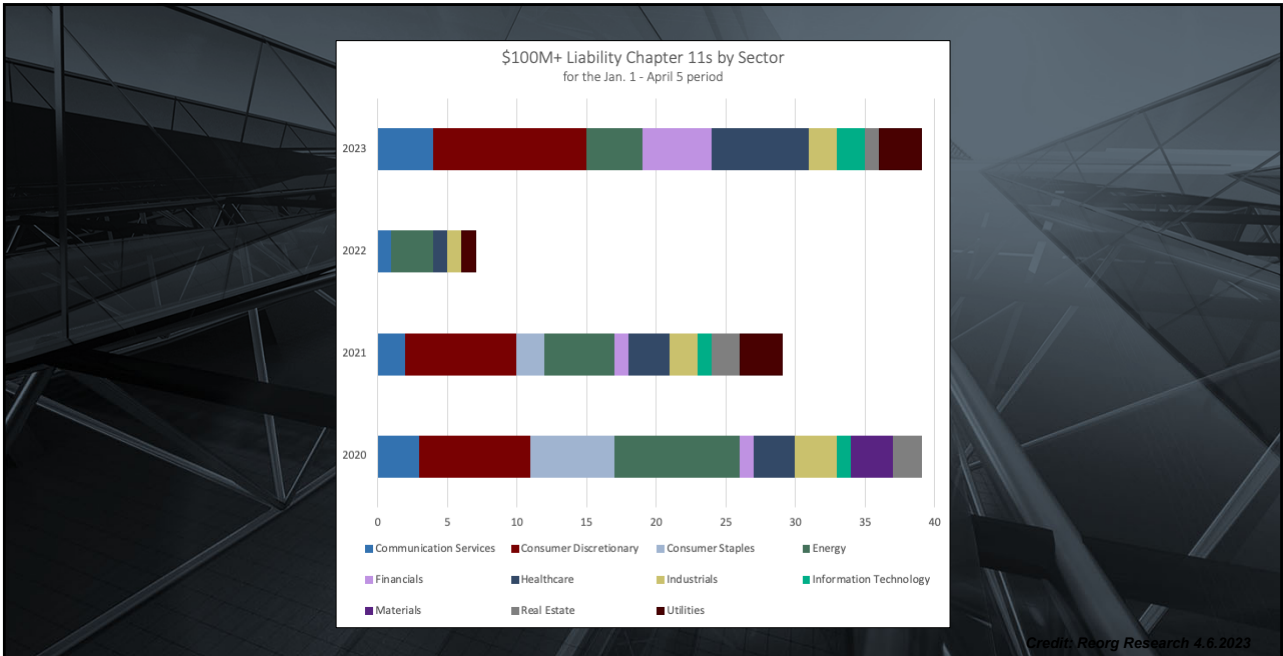


Current Environment

- Tight labor market
- High cost of capital
- Inflation persists
- Supply chains stabilizing in some areas
- Market uncertainty (Silicon Valley Bank, First Republic)
 - Tighter lending market predicted
- Q1 2023: \$10M+ Liability Chapter 11 filings at highest quarterly volume since Q3 2020 and fourth highest since Q1 2016; \$100M+ filings up 457% from 2022 (39 cases through 4/6)



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Agenda

- Pre-bankruptcy Planning and Risk Mitigation
- Bankruptcy Purposes and Case Structure
- Creditors' Committee
- The Automatic Stay
- Critical Vendor Status
- Reclamation Demands
- Claims
- Contract Assumption or Rejection
- IP, Licenses and Consignment
- Preference Actions
- Chapter 11 Plan
- Bankruptcy Sales
- Key Takeaways

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Pre-bankruptcy Planning and Risk Mitigation

Plan for bankruptcy long before there may be a problem

- Understand the result if a vendor, customer, tenant, borrower or other constituent files for bankruptcy

Watch for red flags and act quickly

- Develop a strategy to minimize or eliminate preference exposure
- If you are entitled to financial or other information under your agreements, make sure to ask for it
- If your counterparty is a public company, pay attention to their public filings
- Consider alternatives to enhance your position while minimizing voidable transfer risk
 - Guarantees
 - Cash in Advance
 - Cash on Delivery
 - Letters of Credit
 - Deposit

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Bankruptcy Purposes and Case Structure

- Bankruptcy is a judicially supervised process for the orderly payment of claims and liquidation or reorganization of a financially troubled debtor
- Maintains the status quo and gives a troubled company breathing room
- Orderly liquidation or reorganization vs. piecemeal dismemberment
- Preserves going concern value where possible
- A bankruptcy case is commenced by the filing of a voluntary petition by the Debtor or by an involuntary petition by a creditor or creditors in a Chapter 7 or Chapter 11 case
- Debtor is liquidated or emerges as a reorganized entity
- Process may include sale of the company
- Involuntary bankruptcy



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Creditors' Committee

What is a creditors' committee?

- Formed by the United States Trustee (UST) early in a Chapter 11 case (unlikely in a subchapter V case)
- Ideally represents a cross section of the unsecured creditor body
- UST will send committee solicitation materials to top 20-30 unsecured creditors, including a questionnaire, and then interview interested parties
 - Questions relate primarily to the claim — amount, basis, priority

Why should a creditor serve?

- Information flow
 - As a member of the committee, you have an inside track on that information and receive real-time updates and analysis from committee professionals
- You have a seat at the table to help shape case activity
- You have a fiduciary duty to the committee as a whole
- All fees/expenses of committee members and professionals are paid by the estate



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The Automatic Stay

- The moment that a bankruptcy is filed, an “automatic stay” springs into effect. This is self executing — no notice need be given to subject a party to the automatic stay.
- Prohibits any act to obtain possession or control of property of the estate and prevents creditors from taking any action to collect or recover a claim against the debtor that arose before the bankruptcy filing. Only bars acts against the debtor (i.e., can pursue other parties liable for the debt if they have not filed).
- Prohibited acts include commencement or continuation of litigation, enforcement of a judgment, setoff, lien perfection, default or termination notice.



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CONTINUED

The Automatic Stay

- Timing is key: Claims against the debtor’s estate arising after the bankruptcy filing may be pursued and enforced against the debtor in bankruptcy court (e.g., a post-petition contract default). This often leads to dispute.
- Only a stay — does not toll deadlines that occur during the case (e.g., date by which to exercise option, expiration of a contract).
- If the debtor has done something adverse — breached the lease or contract, failed to pay — that requires you to take some action, you must file a motion with the bankruptcy court for permission to terminate contract/lease or utilize set-off rights.



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Critical Vendor Status

Debtors often seek bankruptcy court approval to set aside a "pot" of money to pay prepetition claims of those vendors they deem "critical"

- Product/service provided by the vendor is essential for day-to-day operations (sole source provider)
- Operating with no enforceable contract (creditor can "walk", but be mindful of Automatic Stay)
- Critical Vendor:
 - Must operate on favorable terms going forward
 - Often can negotiate a payment of some/all prepetition amounts
 - May be able to negotiate a waiver of preference/avoidance actions



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Reclamation Demands

- Special, but limited, right to reclaim goods shipped to the debtor
- Before bankruptcy, have right to reclaim under Uniform Commercial Code 2-207
- After bankruptcy, vendor can make a reclamation demand for goods Debtor received within 45 days of the bankruptcy filing
- If the 45-day period expires after the bankruptcy case is filed, the vendor must make the reclamation demand within 20 days after the bankruptcy filing
- Right to reclaim is lost if debtor sells the goods before or after demand is made
- Right of reclamation is subject to a secured lender's interest in the delivered goods



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Claims

- Filing a claim is an essential part of any bankruptcy. What constitutes a claim in bankruptcy is extremely broad. It includes everything you could possibly imagine, any right to payment, even if contingent, unliquidated and unmatured.
- If the debtor owes you any money, or may at some point in the future (e.g., indemnification), you must file a proof of claim to protect yourself.
- Types of claims vary and often depend on the basis of your claim and when relevant activity occurred — administrative, priority, general unsecured, reclamation or rejection damages.
- The claim is a form:
 - Official Form B410, available online
 - You can supplement with any information you think is relevant



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Contract Assumption or Rejection

- A debtor has three options in bankruptcy with respect to unexpired leases and executory contracts:
 - I. Assume (affirm) its obligations and continue to perform
 - II. Assume and assign the agreement to a third party
 - III. Reject the agreement, which is equivalent to a court-approved breach
- A contract or lease in default (monetary and covenant) must be cured before it can be assumed.
- A contract or lease can be assigned, notwithstanding anti-assignment provisions.



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Contract Assumption or Rejection

Pending assumption or rejection, contract counterparties must perform:

- Debtor is obligated to pay in the ordinary course
- Unpaid post-petition charges must be paid in full in order for a plan to be confirmed
- If debtor fails to pay, counterparty may seek relief from the court to exercise termination rights or to compel assumption or rejection ("stay relief")

What if nothing happens during the bankruptcy?

- A lease will be "deemed" rejected by operation of bankruptcy law
- A contract can be assumed or rejected at the end of the case as part of Chapter 11 plan



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IP Rights, Licenses and Consignment

- Non-debtor licensee: If rejected, can retain the licensee's rights despite rejection (Bankruptcy Code trying to avoid downstream disruption)
- In most jurisdictions, **non-exclusive licenses** generally not assignable over licensor's objection
- Exclusive license can typically be assigned even over objection of non-debtor
- Consigned goods need to be clearly identified, segregated, senior lender exclusions, UCC-1 financing statements
- *If your business is highly dependent on IP licenses or consigned goods, pre-planning can make your life easier*



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Preference Actions

- What is a preference?
 - A payment to a creditor within 90 days of the filing of the bankruptcy on an antecedent debt that allows the creditor to receive more on its claim than it would have if the payment not been made and if the claim was paid through the bankruptcy as a claim
 - No requirement that there be intent to prefer
- If a contract or lease is assumed, there is no preference exposure
- Pre-payments can never be a preference — no antecedent debt



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CONTINUED

Preference Actions

- There are defenses available to creditors:
 - New Value: Have you shipped/provided services after payment received?
 - Ordinary Course: Number of days between invoice/date due and payment
 - Contemporaneous Exchange: Check swapping (C.O.D.)
- Unless you have a new-value defense, which is generally not subject to interpretation, expect to settle these claims. Strength of defense will determine range of settlement payment.



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Chapter 11 Plan

- Disclosure statement approved by the court accompanies the plan sent to creditors and provides a summary of the plan and financial and other relevant information
- Main event of the Chapter 11 case
- Classifies claims and specifies how they will be paid (if at all)
- Can provide for many major corporate events — cancel old equity, issue new equity, sell all assets, mergers, global contract assumption or rejection
- Plan may be approved consensually (two-thirds in amount of claims and one half in number of claims of each class must accept) or by “cram down”



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CONTINUED

Chapter 11 Plan

- Court can only approve if “administrative expenses” (post-petition charges) are paid in full
- Can also contemplate liquidation
- Creditors should review for:
 - Treatment of its existing claims
 - Payment of post-petition obligations
 - Contract issues (assumption, assumption and assignment or rejection)
 - Sale of debtor



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Bankruptcy Sales – Opportunities!

- Section 363 of the Bankruptcy Code allows for the sale of a debtor’s assets (all or substantially all or a smaller subset) **free and clear** of liens, claims and encumbrances (known as “363 Sales”)
- Participation in a 363 Sale can create unique and valuable opportunities for investors and competitors to acquire the assets of distressed companies
- Debtor may assume and assign contracts to buyer notwithstanding non-assignment provisions in agreements (except for certain exceptions)
- Claims against the old entity remain behind in the case unless contract assumed
- Secured creditors may credit bid



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CONTINUED

Bankruptcy Sales – Opportunities!

- Most efficient manner to sell substantially all the company’s assets under the Bankruptcy Code
- Sales processes and solicitation of offers can occur:
 - Wholly inside Chapter 11
 - Outside Chapter 11 with consummation of the deal shortly after a Chapter 11 filing
- Interested buyer may serve as “stalking horse:”
 - Stalking horse bidders set a “floor” for bidding
 - Receive additional bid protections in the form of a break-up fee and/or expense reimbursement and involvement in sale timelines/milestones
- Often, the sale is arranged before the case even files, which results in an accelerated timeline (sales closed within 60 days of the petition date)



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Key Takeaways

- Vigilance is key, particularly pre-petition:
 - Closely monitor AR (watch for customers who start to stretch payments or ask for accommodations)
 - Terminate if necessary
 - Control what you can
 - COVID-19 makes your vigilance even more important
- Set the goal; may depend on whether debtor is liquidating or reorganizing:
 - Do you have a partner for the long haul or is the debtor going out of business?
 - Do you want to cut your losses?
- File your claim, even if you think the debtor is going to assume the lease or contract.
- CHECK THE MAIL!
- Keep the debtor honest. While it's usually a last resort, motion practice may be necessary to enforce obligations, including payment.



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Employee Bankruptcies

What effect does a bankruptcy filing by an employee or former employee have?

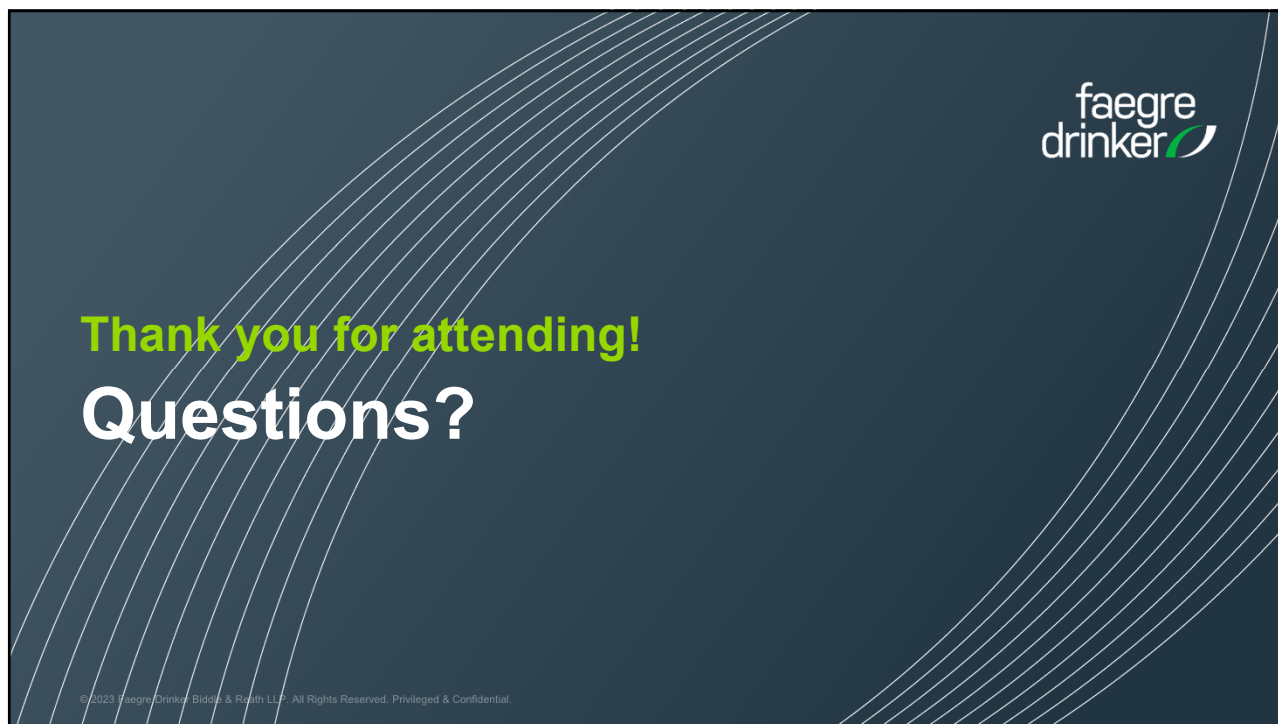
- Garnishment orders
- Employee loans
- Employee litigation

Entry of discharge?



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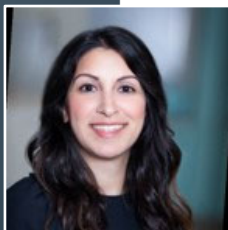
Mike Gustafson represents clients in a full range of financial and corporate matters, including complex financial transactions, corporate debt restructuring, prebankruptcy contingency planning, distressed asset purchases, joint ventures and financial litigation matters. He focuses his practice on bankruptcy and distressed asset matters, regularly assisting clients with Chapter 11 proceedings.

Mike believes that effectively serving his clients requires a curiosity and an interest in learning not just their legal problems but also their business and goals. Mike works hard to develop successful client relationships where clients will not only call when they have problems, but view their Faegre Drinker relationship as a valuable, ongoing collaboration.

Before joining Faegre Drinker, Mike practiced in the Chicago office of an international law firm, where he cultivated high-level transactional and litigation skills in restructuring and bankruptcy. Mike counseled corporate debtors in Chapter 11 proceedings, and creditors and contract counter-parties in distressed situations.



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Candice Korkis is a senior counsel for BMO Financial Group, advising the special assets teams in all facets of commercial lending workouts, including in-court and out-of-court restructurings, and litigation. Prior to joining BMO, Candice was an associate in Skadden's restructuring practice. She is a graduate of the University of Michigan Law School and is admitted to practice in Illinois.



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