

FAST AND FURIOUS: The Breakneck Pace of Chapter 11 and Its Impact On Creditors' Recoveries

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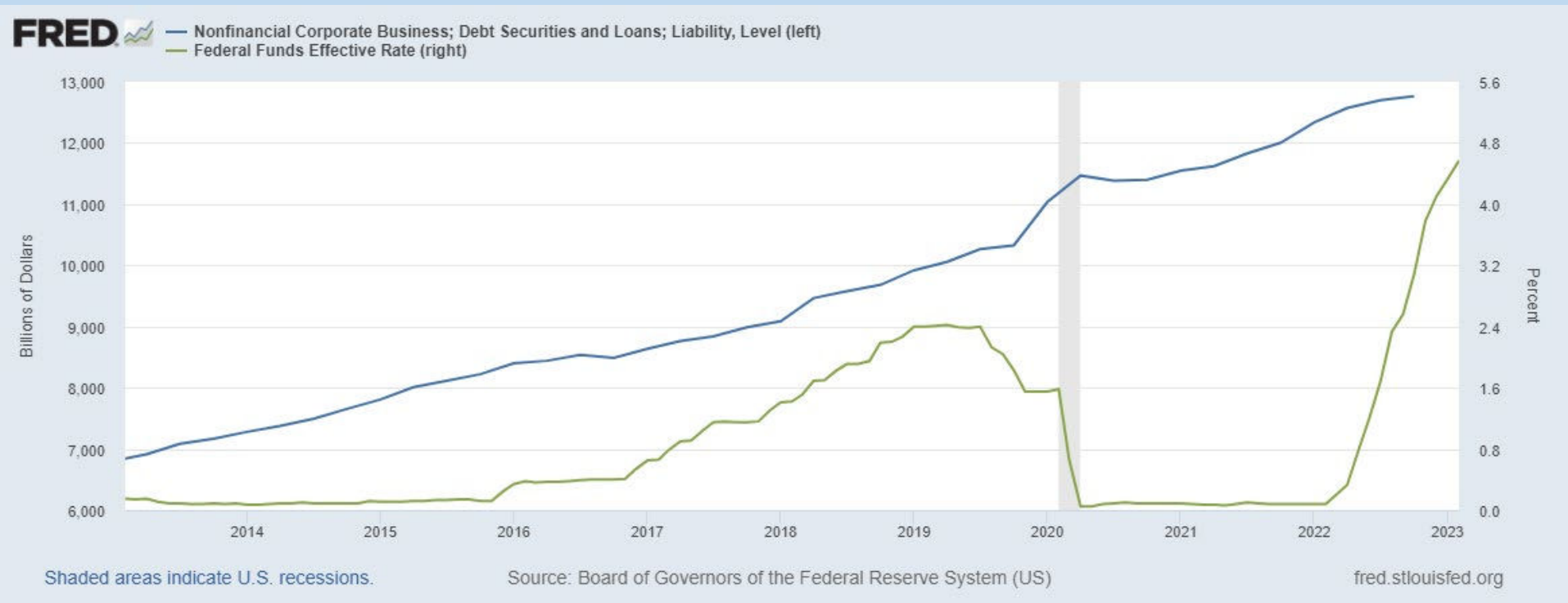
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State of the Union

Selected macroeconomic factors impacting the bankruptcy and restructuring landscape



Corporate debt was at an all-time high pre-pandemic, then grew even more rapidly as interest rates hit all-time lows.



Economic growth has proven stubbornly resilient even in the face of contractionary Fed monetary policy... but will it last?



Leading Indicator: 10y-3m Treasury yield curve is **more deeply inverted** than it has been in 40 years.



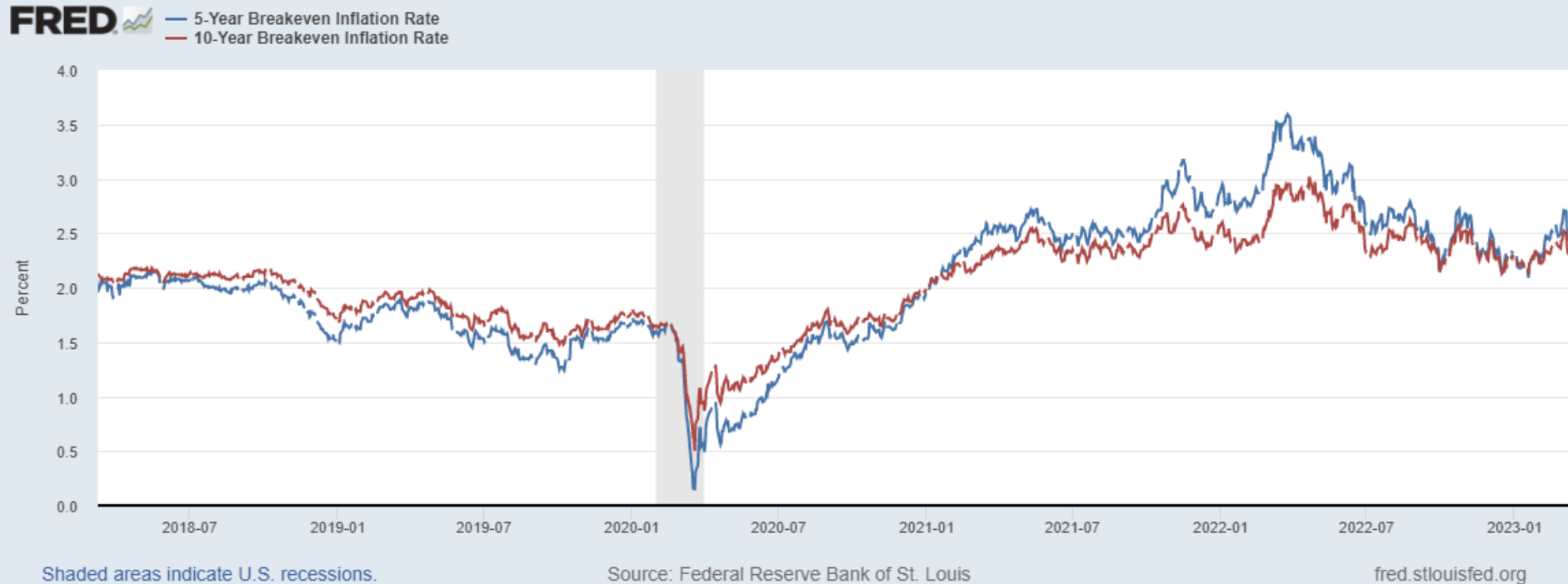
Leading Indicator: 10y-2y Treasury yield curve is deeply inverted, but not (yet?) as deeply as in some prior recessions.



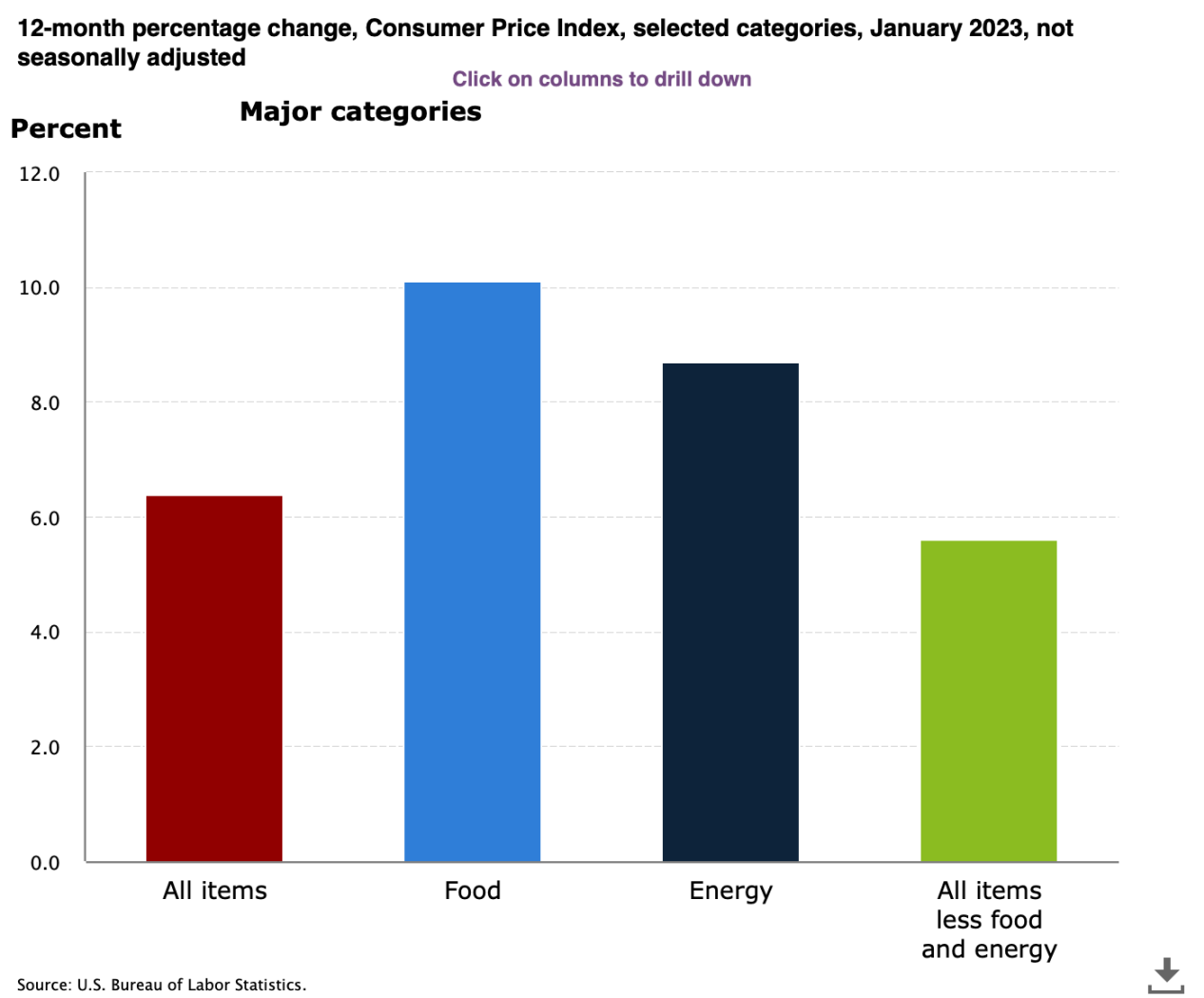
TIPS Spreads continue to suggest above-average inflation will be around for a while, but not forever.



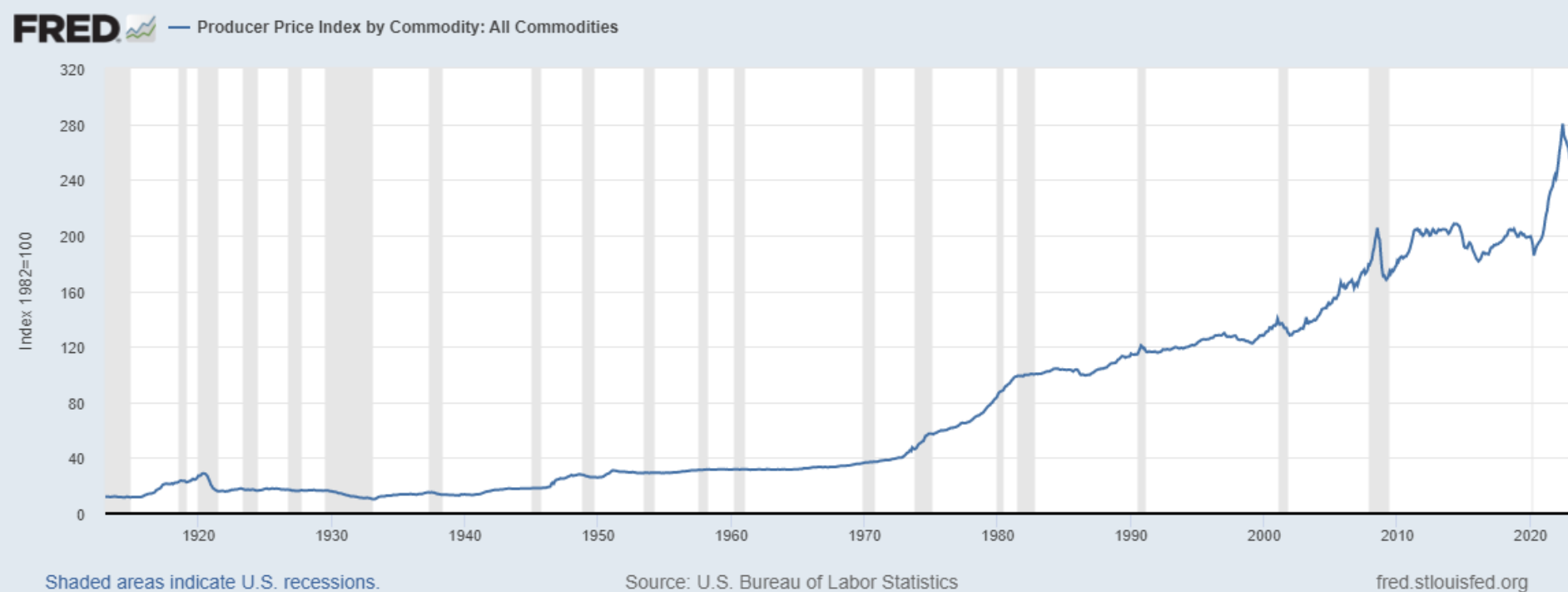
TIPS Spreads continue to suggest above-average inflation will be around for a while, but not forever.



CPI inflation persists across all components, with energy remaining the most significant driver.



Producer prices have come down but have not yet stabilized. Stubborn energy costs are likely to blame, in large part.



Labor force participation remains depressed relative to pre-COVID levels.



The number of working-age Americans not in the labor force remains significantly elevated, and probably won't change soon.



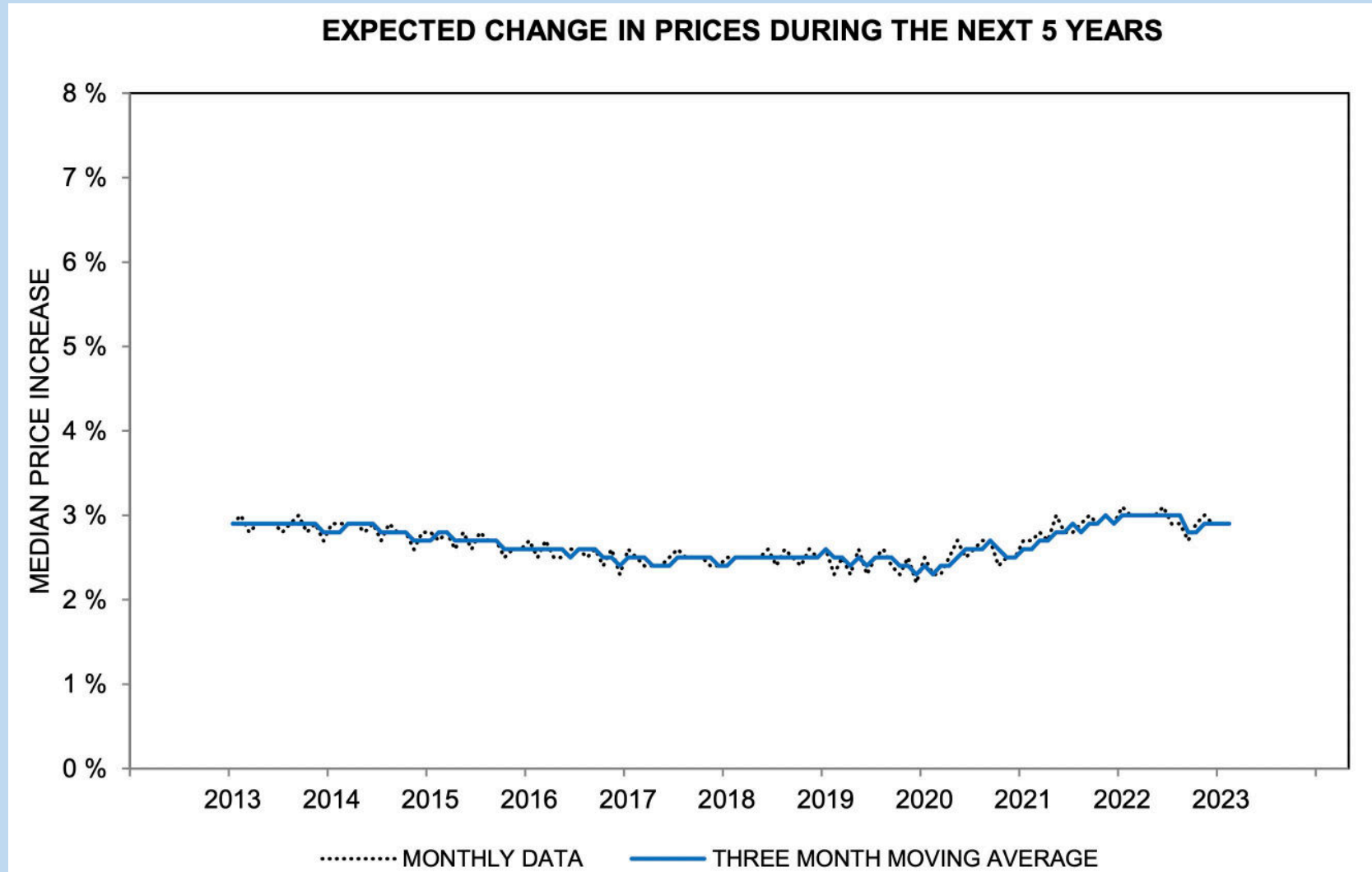
As a result, labor demand continue to outstrip supply, thwarting the Fed's efforts to cool inflation.



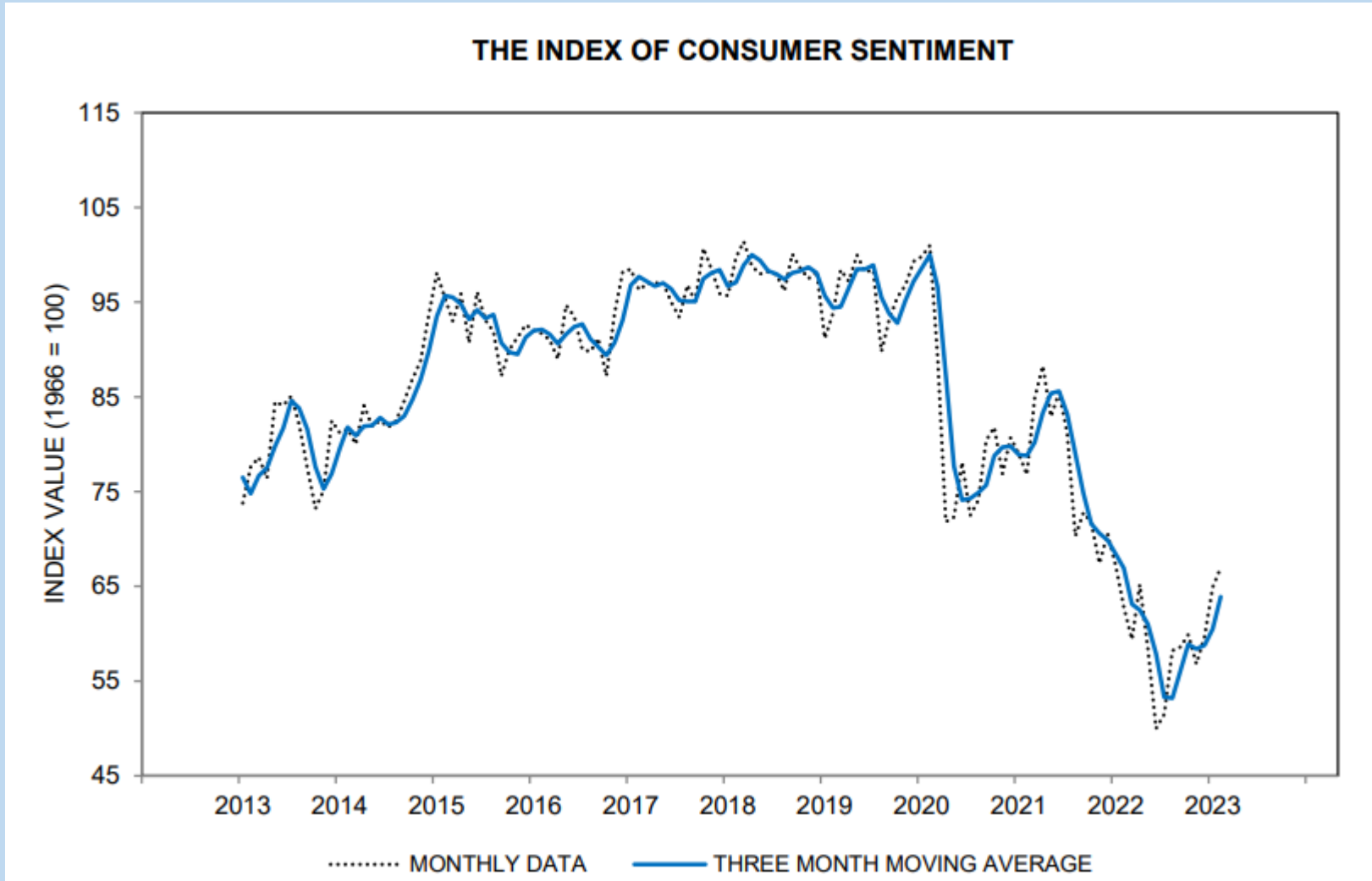
Consumers' expectations of inflation have tapered off in the last few months but remain significantly elevated.



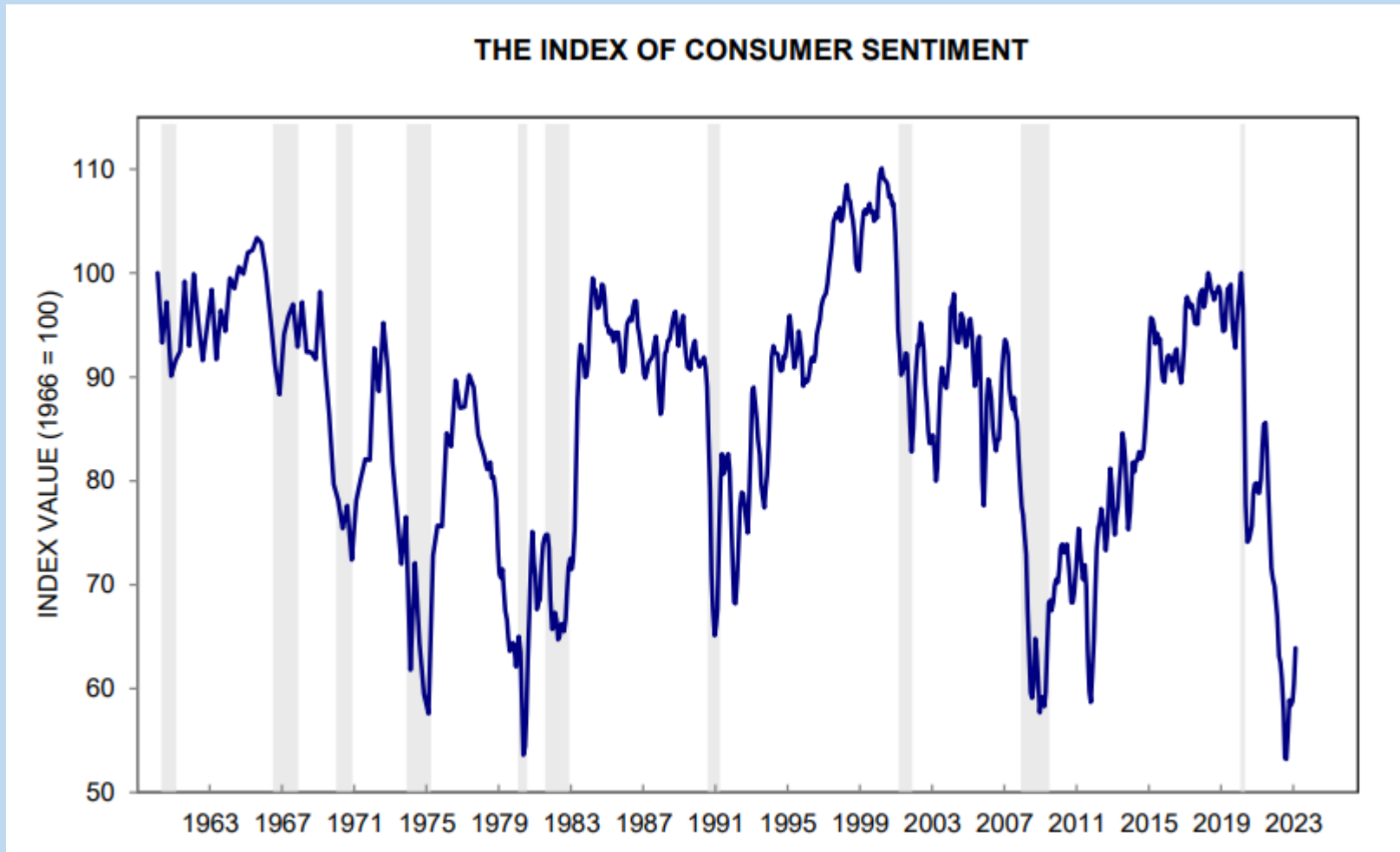
Longer-term inflation expectations remain slightly elevated, but to a much lesser degree than their views of near-term inflation.



Paradox? Consumer sentiment has rebounded somewhat but remains significantly depressed relative to pre-COVID periods.



...but consumer sentiment remains relatively near its all-time, pre-COVID lows.



What does all this add up to?

Multiple factors simultaneously putting pressure on the global economy likely are driving a significant uptick of Chapter 11 bankruptcy filings in 2023, including, among others:

- High inflation
- Fed contraction, including increased interest rates
- Continued supply chain disruptions
- Labor shortages and rising labor costs
- Rising commodity prices
- End of business stimulus programs
- Excessive leverage incurred during 2020-2022
- Increased refinancing risk due to increasing rates
- Geopolitical tensions
- Recession risk

Significant Increase in Chapter 11 Filings

- Increase in Chapter 11 Filings in Second Half of 2022
- Accelerated Chapter 11 Filings so far in 2023
 - Approximately **78% increase** in commercial chapter 11 filings through February 2023 vs. same period in 2022

	<u>2023</u>	<u>2022</u>
January	257	151
February	<u>373</u>	<u>204</u>
Total	630	355

- Approximately **47% increase** in Subchapter V filings through February 2023 vs. same period in 2022

	<u>2023</u>	<u>2022</u>
January	137	92
February	<u>120</u>	<u>83</u>
Total	257	175

The Road Ahead: Chapter 11 After the COVID-19 Pandemic

Trends (old and new) and other changes to the Chapter 11 landscape



■ A Dizzying Pace : The Era Of Speedier Chapter 11

- Chapter 11 Has **Radically Changed** in 20 (Even 10) Years
 - True restructuring – fix operational issues *and* deleverage the balance sheet – is **now the exception**, not the norm
 - Faster process is now the norm:
 - Prepackaged Plans
 - Prearranged Plans
 - **Asset Sales** are no longer just a fallback



■ Why?

- Significant increase in balance sheet leverage from 2020-2022
- Prevalence of private equity and hedge fund ownership
- Lack of lender patience: **get paid and run**
- Increase in **loan-to-own** distressed lending
- Chapter 11 administrative costs have ballooned

Prepackaged vs. Pre-Negotiated Chapter 11 Plans

Prepackaged (“Prepack”)

Plan has been **solicited in advance** and **accepted by voting classes**

Confirmation occurs very quickly – sometimes 60-90 days post-filing

Belk: Drive-through chapter 11 (in and out of bankruptcy in 24 hours!)

Trade claims **typically paid in full** after confirmation or per their terms

Pre-filing vote solicitation provides (near) certainty that impaired, objecting classes will be crammed down

Typically no creditors’ committee

Minimal risk of administrative insolvency

Preference claims *usually* waived

Minimal operational disruption

Pre-negotiated

Plan Support Agreement (PSA) has been **negotiated with certain classes**

Plan still needs to be filed and votes solicited – may take months or years

Caesars: Took *nearly two years*

No certainty as to treatment of trade claims – **typically impaired**, sometimes severely. Critical vendors may be treated better.

No certainty as to how any creditors besides the PSA parties will vote – objecting creditors may hijack process

Almost always a creditors’ committee

Risk of administrative insolvency

No certainty re: preference waiver

Risk of significant operational disruption

Section 363 Sales

- Debtor Uses Bankruptcy Code Section 363 to Sell Assets
 - Entire business, specific assets / business lines, GOB sales
- Sales Under Section 363 Allow the Buyer to Obtain Court Approval To Purchase a Set of Specific Assets Free and Clear of Liens, Claims and Encumbrances Faster Than Through A Reorganization Plan
 - Bankruptcy sale process is public, benefitting debtor and creditors, and the sale is subject to higher and better offers, auction, court approval
 - “Higher and better” contemplates not only the purchase price, but other factors: form and terms of APA, form of consideration, ability to close, continued employment (preserving jobs) vs. liquidation
- Credit Bid: Ability of a secured lender to bid with its secured claim instead of new cash – up to 100% of the par amount of its debt (!)
 - Often part of a loan-to-own strategy
 - Can deter competitive bidding
- Creditors’ Committee May Be Only Check on Process
- Increased Frequency of Structured Dismissals as Exit Strategy in Administrative Insolvency Cases

Freefall Chapter 11 Cases

- Debtor files Chapter 11 Petition Without Negotiated Restructuring Terms With any of its Key Stakeholders
 - Example, Revlon: No Restructuring Support Agreement Setting Case Deadlines and Prescribing Chapter 11 Plan Terms
- Deferral of Agreed Chapter 11 Plan Terms That Would Permit Debtor to Exit Chapter 11 Until
 - Debtor stabilizes its business
 - Debtor avails itself of following benefits of chapter 11 to address operational issues
 - Automatic stay
 - Rejection of unprofitable contracts and leases
 - Sale of or exit from unprofitable business units



Case Study – Revlon

REVLON®

MOST RECENT FREEFALL CHAPTER 11 MEGA CASE

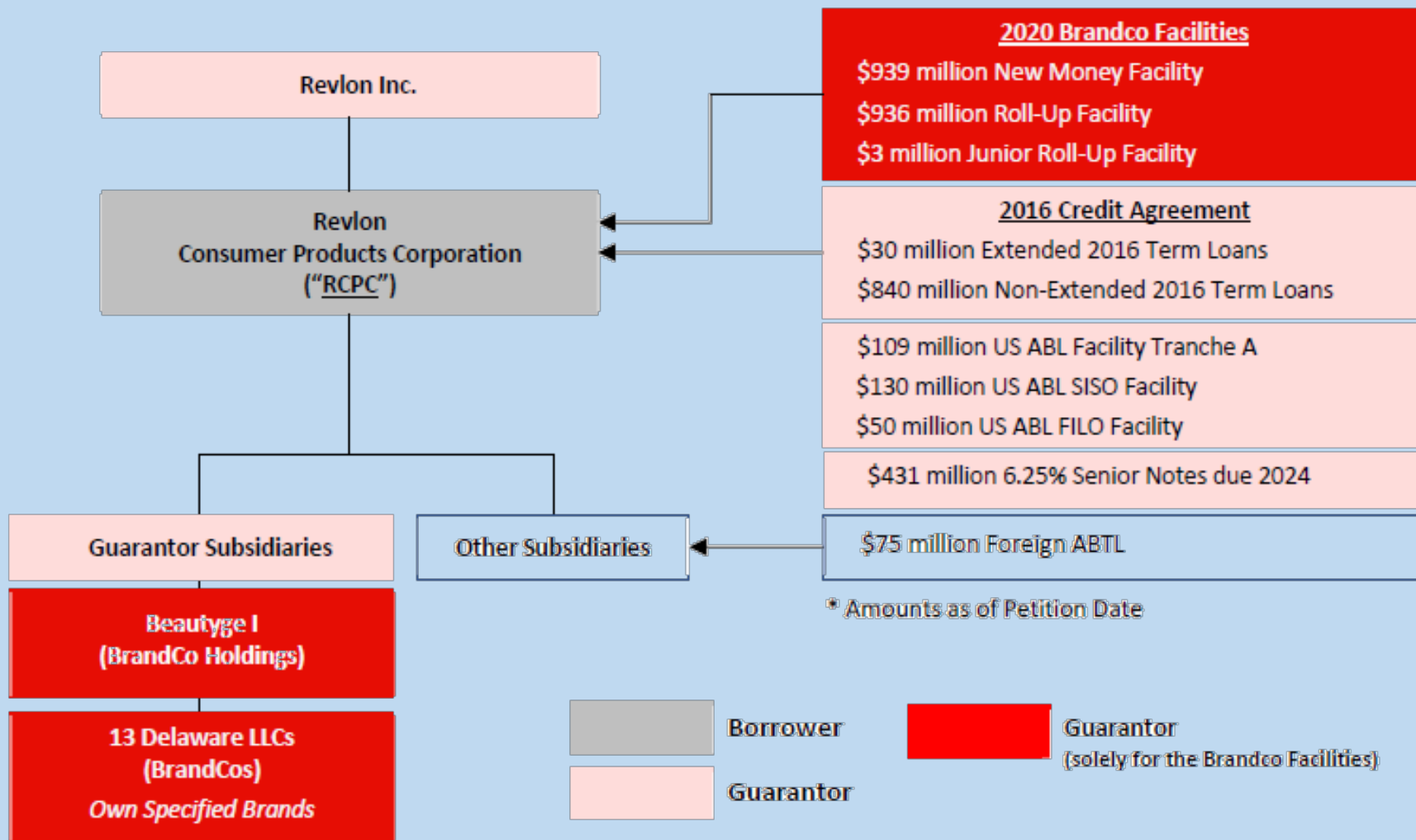
- Global Leader in Beauty Industry With More than 20 Key Brands
 - Revlon
 - Elizabeth Arden
- Revlon Filed Chapter 11 in Southern District New York Bankruptcy Court on June 15, 2022
- Causes for Filing
 - “Significantly constrained liquidity” since onset of COVID-19 pandemic
 - Industry headwinds and macroeconomic issues, including supply chain disruptions, inflation and volatility in the capital markets
 - Inability to obtain and produce sufficient inventory
 - Labor shortages
 - Loss of trade credit, increased frequency of cash in advance terms
 - Overleveraged and Complicated Capital Structure and Significant Intercreditor Disputes

Case Study – Revlon

MOST RECENT FREEFALL CHAPTER 11 MEGA CASE

Instrument / Facility	Principal Outstanding
US ABL Facility	
Tranche A Revolving Loans	\$109,000,000
ABL FILO Term Loans	\$50,000,000
SISO Term Loan Facility	\$130,000,000
Total US ABL Facility	\$289,000,000
BrandCo Facilities	
First Lien BrandCo Facility	\$938,986,931
Second Lien BrandCo Facility	\$936,052,001
Third Lien BrandCo Facility	\$2,980,287
Total BrandCo Facilities	\$1,878,019,219
2016 Term Loan Facility	\$870,116,570 ³
Unsecured Notes	\$431,300,000
Foreign ABTL Facility	\$75,000,000
Total Indebtedness	\$3,543,435,789

Case Study – Revlon: Funded Debt



Revlon: Intercreditor Disputes

■ Citibank Mistaken Payment Litigation

- 3 groups
 - Citibank; mistakenly paid approximately \$885 million to holders of 2016 senior secured term debt
 - Lenders owed approximately \$385 million that returned mistaken payments
 - Lenders owed approximately \$500 million that refused to return mistaken payments subject to Citibank lawsuit seeking recovery of payments
- February, 2021, U.S. District Court, Southern District of New York ruled that Lenders refusing to return mistaken payments could keep the funds paid
- Appealed to U.S. Court of Appeals for the Second Circuit; held Citibank entitled to return of mistaken payments based on defendants' constructive notice of Citibank's error and 2016 senior secured term debt not yet due
 - Non-returning lenders moved for rehearing by the entire Second Circuit
 - Motion denied on November 11
- Resolution of prior uncertainty as to who speaks for the 2016 senior secured term loan group?



■ Revlon: Intercreditor Disputes (cont'd)

- Brandco Transactions and Secured Loan Facility (Subject to Challenge)
- In early 2020, Revlon Transferred Most of its Intellectual Property, Including Many Valuable Brands, to the Brandco Entities (also Chapter 11 Debtors), Subject to License Back to Revlon operating entities
- Brandco Lenders (Subset of Holders of 2016 Senior Secured Term Debt) Then Made Advances to Debtors and Were Owed \$1.88 Billion on the Petition Date
 - Secured by first priority liens on transferred intellectual property
 - Revlon operating entities became liable on the Brandco loans as borrowers or guarantors, secured with senior liens in Revlon assets which shared *pari passu* with the liens securing 2016 Senior Term Loan Facility

■ Revlon: Intercreditor Disputes (cont'd)

- Net Result of Brandco Transactions/Secured Loans
 - Valuable intellectual property rights siphoned off from Revlon/Operating Subsidiaries
 - Revlon/Operating Subsidiaries primarily liable to Brandco secured lenders and for royalty payments due under licensing agreements with Brandco entities
 - Non-Brandco 2016 senior secured term lenders and other non-Brandco secured lenders, unsecured creditors and tort victims subordinated to Brandco secured lenders in the Debtors' capital structure by approximately \$1.7 billion

Revlon: DIP Financing

- Includes Brandco Secured Lenders
 - \$400 million ABL facility
 - \$575 million term loan facility
 - Super priority junior secured intercompany facility with Brandco debtors
- Relevant Milestones
 - November 1, 2022: entry into restructuring support agreement related to acceptable chapter 11 plan
 - November 30, 2022: Filing of acceptable Chapter 11 plan and disclosure statement
 - April 1, 2023: entry of order confirming acceptable chapter 11 plan
 - April 15, 2023: substantial consummation of acceptable confirmed chapter 11 plan



■ Revlon: DIP Financing Objection

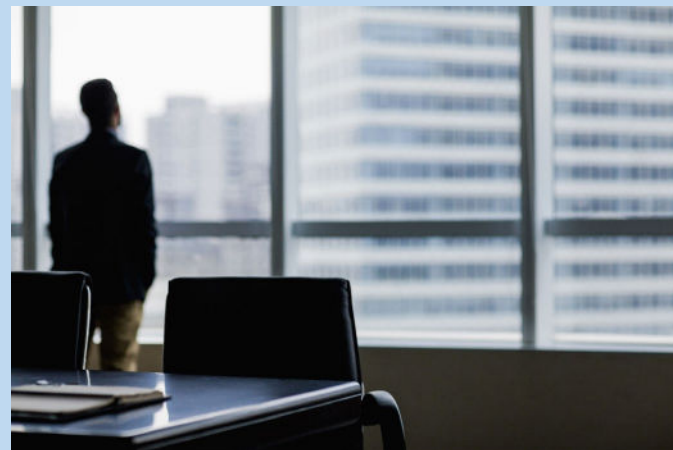
- Creditors' Committee Objected to Financing
 - Revlon chapter 11 cases “one of the largest and most important bankruptcies in America” and “a mess”
 - No idea of Debtors' value
 - Questioned Debtors' re-engineered capital structure resulting from the 2020 Brandco Transactions and Secured Loan Facility
 - “Fleeced unsecured creditors at the legacy Revlon companies for the benefit of the Brandco lenders, some of whom “traded up” their legacy debt position into the Brandco secured loan facility, and improved their position in Revlon's capital structure
 - Questioned the grant of liens on the proceeds of avoidance actions that would include any lawsuit to unwind the Brandco transactions and secured loan facility

■ Revlon: Bankruptcy Court's Final Approval of Financing

- Court Deferred to Debtors' Business Judgment on Financing Terms
- Broad Reservation of Rights in Financing Order that Protected all Parties' Ability to Challenge 2020 Brandco Transactions and Secured Loan Facility
 - Debtors argued that was the reason that Citibank and the 2016 senior secured term lenders did not object to DIP financing
- Brandco Secured Lenders also Agreed to 15 Day Extensions of Deadline for Agreed Restructuring Support Agreement to November 15, 2022 and of Deadline for Filing Acceptable Plan and Disclosure Statement to December 14, 2022

Revlon: Critical Vendor Order

- Bankruptcy Court Approved Final Critical Vendor Order
 - Authorized but did not direct Debtors to pay \$79.4 million of Vendor Obligations
 - Brandco secured lenders and creditors' committee granted consultation rights
 - Debtors must provide committee with vendor agreements including materially different terms than terms provided in sample vendor agreement attached to critical vendor motion and/or including waiver of debtors' claims, such as preference claims, against a vendor
 - Each Friday, Debtors obligated to deliver to Brandco secured lenders and committee vendor agreements executed the prior week and a report of all payments to critical vendors
- Critical Vendors Must Provide "Customary Terms" and Risk Disgorgement of Critical Vendor Payments if they Fail to Provide Such Terms
- Debtors Can Settle claims (including preference claims) against any Vendor Subject to Prior Consent of Brandco secured lenders and Committee



Revlon: Ad Hoc Shareholder Group's Motion For Appointment Of Official Equity Committee

- Revlon's Stock Price Traded at \$8.38 Per Share on August 8, 2022
 - Reflected market capitalization of \$457 million
 - Market appears to be concluding Revlon is solvent
 - Revlon not hopelessly insolvent
 - Stock price expected to further increase if disputed claims are disallowed
 - Stock price as of September 14, 2022: \$6.43 per share
- Equity Should be Further in the Money if Certain Disputes regarding Citibank's Payments of Revlon's 2016 Senior Secured Term Lenders and Revlon's Exposure to Asbestos-Related Personal Injury Claims are Addressed



Revlon: Objections to Motion for Appointment of Equity Committee

■ Debtors' Objection

- No substantial likelihood that equity will receive meaningful distribution
 - Trading price of debtors' unsecured notes as low as 10 cents on the dollar
- Per Debtors' most recent 10Q filing as of June 30, 2022, stockholders' equity had \$2.34 billion deficit
- Other well-funded parties, such as the Debtors, ad hoc shareholder group, Debtors' majority (85%) shareholder, creditors' committee and other parties aligned with stockholders' interests



Revlon: Additional Objections to Appointment of Official Equity Committee

■ Creditors' Committee's Objection

- Neither stock nor debt trading prices are relevant
- Debtors' stock trading has all the outward appearances of a meme stock



■ Brandco Secured Lenders Objection

- Debtors' stock price subject to recent and significant fluctuations that “appear untethered from market realities”

Revlon: Bankruptcy Court's Denial of Appointment of Official Equity Committee

- Ad hoc Stockholder Group Failed to Prove:
 - Substantial likelihood of a meaningful recovery to stockholders
 - Necessity of an official equity committee to adequately represent stockholders in the chapter 11 cases
- Costs of Official Equity Committee Would be Burdensome on the Estate
- Equity Committee Would Duplicate the Work of the Creditors' Committee
- Current Stock Price Supports Court's Ruling: \$.66 per share as of February 17, 2023

2016 Secured Term Lenders' Complaint vs. Brandco Lenders and Revlon

- Filed October 31, 2022
- Sought Following Relief
 - Unwind transfer of valuable intellectual property to Brandco
 - Restore 2016 Secured Term Lenders to their rightful first lien position in Brandco IP
 - Recovery of monetary damages
- Revlon and Brandco Lenders Moved to Dismiss Complaint
 - 2016 Secured Term Lenders opposed dismissal of complaint
 - Motion to dismiss argued on February 2, 2023
- Trial Scheduled for March 6, 2023

Chapter 11 Plan Process

- Revlon filed Chapter 11 Plan and Disclosure Statement on December 23, 2022
- Intended to Implement a Restructuring Support Agreement/Settlement Among the Brandco Lenders, Revlon and the Unsecured Creditors' Committee
- Based on \$1.6 Billion Equity Value for Revlon Business
 - Includes \$400 Million of exit financing
 - Includes an equity rights offering of \$650 million for 70% of new Revlon stock



Dissenting 2016 Secured Term Lenders' Objection to Disclosure Statement

- Proposed Plan “Represents the Culmination of a Brazen Multi-Year Scheme That Violates the Bankruptcy Code and Governing Contracts”
- Plan is Patently Unconfirmable
 - Premised on improper gerrymander/classification by including Brandco lender claims against operating Revlon entities in same class as dissenting 2016 Secured Term lenders to assure class acceptance
 - Violates the absolute priority rule by providing settlement payments to unsecured creditors before 2016 Secured Term Lenders are paid in full

■ Global Settlement Involving 2016 Secured Term Lenders

- Court Granted Revlon's Motion to Dismiss 2016 Secured Term Lenders'
- Hearing on Approval of Disclosure Statement and Other Plan-Related Motions Had Been Adjourned Several Times and Went Forward on February 21, 2023
- Global Settlement Reached Among Revlon, Brandco Lenders and 2016 Secured Term Lenders

Global Settlement Claims Recoveries

- Treatment of Classes of Claims/Estimated Plan Recovery
 - FILO ABL Lenders/100%
 - 2020 Term B-1 Loan Claims (Brandco First Lien)-principal amount of take back term loans or cash in amount of claims/100%
 - 2020 Term B-2 Loan Claims (Brandco Second Lien)-*pro rata* share of 82% of new common stock and right to purchase *pro rata* share of 70% of new Revlon common stock sold pursuant to equity rights offering
 - Estimated recovery range: 44.1% to 87.2%
 - Brandco Third Lien Guaranty/0%

Global Settlement Claims Recoveries

- Treatment of Classes of Claims/Estimated Plan Recovery (cont'd)
 - **Opco Term Loan-2016 Secured Term Lenders/16.8% to 43% (improved from 9% to 12%) recovery largely from Brandco second lien recovery and also from Brandco first lien recovery**
 - Unsecured Notes/12-18%
 - Talc Personal Injury/11-32%
 - Non-qualified pension/15-17%
 - Trade/14-19%
 - Other Unsecureds/13-20%



Chapter 11 Plan Process Global Settlement

- On February 21, 2023, Court Approved Amended Disclosure Statement Reflecting Latest Global Settlement and Other Plan Related Documents
- Plan Confirmation Timetable
 - March 20-Voting deadline
 - March 23-Plan objection deadline
 - April 3-Plan confirmation hearing (deadline April 4)
 - April 18-Plan effective date deadline

■ Subchapter V Small Business Cases

- Enacted as Part of Small Business Reorganization Act of 2019 (SBRA)
 - Purpose is to reduce costs and increase efficiency
 - Permitted any business with maximum aggregate debt of \$2,725,625 to file as a small business Chapter 11; increased to \$3,024,725 on April 1, 2022
- Per CARES Act, the Maximum Aggregate Debt Limit for Small Businesses (Excluding Affiliates/Insiders) Increased to \$7,500,000, Not Less Than 50% From the Debtor's Commercial or Business Activities
 - The Bankruptcy Threshold Adjustment and Technical Corrections Act was signed on June 21, 2022 by President Biden
 - Preserved \$7.5 million eligibility threshold with 2 year sunset on June 21, 2024



■ How is Subchapter V Faring?

- Total Subchapter V Cases Filed Through March 1, 2023: 4,631
 - Number of filings in 2020: 1,360
 - Total filings in 2021: 1,426
 - Total filings in 2022: 1,553
 - Total filings through March 1, 2023: 292
- Largest Number of Subchapter V filings in Eleventh, Ninth, and Fifth Circuits (in descending order)
- Subchapter V Cases Represent a Significant % of All Chapter 11 Filings

■ How is Subchapter V Faring? (cont'd)

- Most Eligible Debtors Have Elected Subchapter V
- Industries Where Subchapter V Has Been More Widely Utilized:
 - Retail
 - Health care
 - Restaurants/Bars
 - Construction
 - Hotel/Lodging
 - Trucking/Transportation
- Subchapter V Cases Appear to be Working as Intended Based on Preliminary Data
 - Subchapter V Debtors confirming plans more quickly and at higher rate than pre-SBRA
 - Improved confirmed plan success rate, at least so far

■ QUESTIONS?

Q&A

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With more than 40 years of experience in the bankruptcy and insolvency field, Bruce is a recognized leader nationwide in trade creditor rights and the representation of trade creditors in bankruptcy and other legal matters. He has represented trade and other unsecured creditors, unsecured creditors' committees, secured creditors, and other interested parties in many of the larger Chapter 11 cases that have been filed. Bruce also handles letters of credit, guarantees, security, consignment, bailment, tolling, and other agreements and legal credit issues for the credit departments of institutional clients.

Among his various legal recognitions, Bruce received the Top Hat Award in 2011, a prestigious annual award honoring extraordinary executives and professionals in the credit industry. He was co-chair of the Avoiding Powers Committee that worked with the American Bankruptcy Institute's (ABI) Commission to Study the Reform of Chapter 11, participated in ABI's Great Debates at their 2010 Annual Spring Meeting—arguing against repeal of the special BAPCPA protections for goods providers and commercial lessors—and was a panelist for a session sponsored by ABI. He is a frequent presenter at industry conferences throughout the country, as well as a prolific author regarding bankruptcy and creditors' rights topics in various legal and trade publications.

Bruce is a co-author of "Trade Creditor's Risk-Mitigation Tools and Remedies Manual," published by ABI in 2019. He has also contributed to **ABI Journal** and is a former member of ABI's Board of Directors and former co-chair of ABI's Unsecured Trade Creditors Committee.



Education

- University of Pennsylvania Law School (J.D. 1980)
- Wharton School of Finance and Business (M.B.A. 1980)
- University of Rochester (B.A. 1976), Phi Beta Kappa

Bar Admissions

- New York

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Andrew leverages his background in corporate finance and management to approach restructuring problems, both in and out of court, from a practical, results-oriented perspective. With a focus on building consensus among multiple parties that have competing priorities, Andrew is equally at home both in and out of the courtroom, and he has a track record of turning financial distress into positive business outcomes. Clients value his counsel in complex Chapter 11 cases, where he represents debtors, creditors' committees, purchasers, and investors.

Andrew writes and speaks frequently about bankruptcy matters and financial issues. Before becoming a lawyer, he worked in senior financial management at a midsize, privately held company.



Education

- Seton Hall University School of Law (J.D. 2009), magna cum laude; Order of the Coif
- University of Missouri-Saint Louis (B.S. 2005), Business Administration-Finance and Accounting; *Beta Gamma Sigma*

Bar Admissions

- New Jersey

Recent Publications and Insights

- January 2023
[UCC Financing Statement Mistakes Can Be Deadly](#), *Business Credit*
Bruce S. Nathan, Michael Papandrea
- December 2022
[Circuit Ruling Expands Subsequent New-Value Preference Defense](#), *ABI Journal*
Bruce S. Nathan, Scott Cargill
- November/December 2022
[A Victory for the Trade: Décor Holdings Decisions Uphold Applicability of Subjective Ordinary Course of Business Defense to Preference Liability](#), *Business Credit*
Bruce S. Nathan, Michael Papandrea
- October 24, 2022
Video: [The Obligations and Responsibilities of Creditors' Committees in Crypto Bankruptcies](#)
Andrew Behlmann, Phillip Khezri
- September/October 2022
[Trade Creditors Have Their Cake and Eat It Too!](#), *Business Credit*
Bruce S. Nathan, Michael Papandrea
- September 13, 2022
Video: [Part 2: Additional Implications for Cryptocurrency Companies in Bankruptcy](#)
Andrew Behlmann, Phillip Khezri
- September 7, 2022
Video: [Crypto Considerations in Bankruptcy Plans of Reorganization](#), *Bankruptcy & Restructuring Department Client Alert*
Jeffrey Cohen, Andrew Behlmann, Phillip Khezri
- July/August 2022
[More 'Goods' News for the Trade](#), *Business Credit*
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