turnarounds & workouts

News for People Tracking Distressed Businesses

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2017 Outlook

Restructuring Challenges and Opportunities Await

by Julie Schaeffer

Last month, we looked back at the events that shaped the restructuring industry in 2016. This month, we look ahead. How will 2017 restructuring activity compare to prior years? Which sectors will see the most activity? What will be the greatest challenges? And are there any unexpected areas to watch?

We asked six bankruptcy professionals: Greg Charleston, senior managing director at Conway MacKenzie; Benjamin Feder, special counsel with Kelley Drye & Warren; Douglas S. Mintz, an attorney at Orrick, Herrington & Sutcliffe; Michael Rosenthal, co-chair of Gibson Dunn's business restructuring and reorganization practice group; Zachary

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Focus on Reclamation

Delaware Court Splits with Southern District of NY

by Randall Reese

Judge Mary Walrath of the United States Bankruptcy Court for the District of Delaware recently ruled on the validity of an administrative claim for a creditor's reclamation rights under section 546(c) of the Bankruptcy Code. In overruling an objection to the claim, Judge Walrath rejected a line of decisions from the Southern District of New York bankruptcy court and was instead persuaded by a decision from the Sixth Circuit Court of Appeals. "While bankruptcy courts have tended to chip away at reclamation claimants' rights, reclamation claims still remain a tool for suppliers to maximize recovery in Chapter 11 cases," according to Jill Nicholson of Foley & Lardner. "In light of *Reichhold*, Delaware offers a more vendor-friendly forum than New York."

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Third Circuit Reverses

Make-Whole Payment Enforced in EFH Bankruptcy

by Julie Schaeffer

The Third Circuit Court of Appeals has reversed bankruptcy and district court opinions in refusing to allow Energy Future Holdings Company (EFH) to use a Chapter 11 filing as a means to reduce interest on its debt obligations.

EFH, along with EFIH Finance Inc., borrowed more than $4 billion at a 10% interest rate by issuing notes secured by first- and second-priority liens on the entities' assets.

According to the indenture governing the loans, EFH could redeem all or part of the notes at 100% of the principal amount plus an "applicable premium" and interest. This "applicable premium was a make-whole premium, designed to the lenders for the interest

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Outlook, *from page 1*

Smith, a member of Moore & Van Allen's bankruptcy and financial restructuring team; and Michael J. Venditto, a partner in the financial industry group at Reed Smith.

What do you think we'll see in 2017?

Charleston: We will likely see several new things in the turnaround and restructuring world in 2017. For example, unitranche lending is a somewhat new lending concept that has evolved over the last several years. A unitranche loan essentially brings different layers of debt together under one loan agreement. In 2017, we may get to see how different examples of unitranche lending arrangements hold up when borrowers become distressed.

Feder: There will be fewer energy-related bankruptcies, as commodity prices have stabilized and are trending upwards. Retail cases will again be a primary sector of activity, beginning with Sears. After that, a lot will depend on the economic policies of the incoming administration and Congress.

Mintz: We will see less distress in 2017 (at least the first half) than we saw in 2016. The oil/gas peak has passed for now. More activity may come down the road there, but for the time being the situation has stabilized. It remains to be seen whether the economy will continue to get frothier before a real upturn comes to distress. Brick-and-mortar retail will undoubtedly remain bound by fundamental problems related to the Internet. There will more retail distress next year. While 2017 may shape up as a year of less distress, it will set the stage for an inevitable downturn to come.

Smith: We will continue to see complex and first-impression legal issues stemming from Puerto Rico's efforts to achieve comprehensive economic growth, fiscal reform, and debt restructuring, as the PROMESA process moves ahead. In addition, I believe we will continue to see an increasing number of early-stage businesses, with unique and promising business ideas applying creative uses of Chapter 11 in order to preserve and maximize going concern value when venture capital or other short-term funding is no longer available.

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Reclamation, *from page 1*

Reichhold Holdings US, Inc. – the debtor in the Chapter 11 case giving rise to Judge Walrath's recent opinion – filed for bankruptcy protection in September 2014. At the time the company filed for bankruptcy, Reichhold was a borrower under a prepetition credit facility with Oaktree Capital Management, L.P. and had entered into a security agreement that granted the lender a lien in substantially all of Reichhold's assets, including inventory. Following the filing, the bankruptcy court approved Reichhold's entry into debtor-in-possession financing agreements, pursuant to which the prepetition Oaktree loan was paid in full from the proceeds of the DIP loan. The DIP loan was secured by a first priority lien on all prepetition and postpetition property of Reichhold's estate, including inventory, but did not attach to property that was "subject to valid, perfected and nonavoidable liens (or to valid liens in existence as of the Petition Date that are subsequently perfected as permitted by section 546(b) of the Bankruptcy Code)."

The creditor whose claims are at issue in Judge Walrath's decision – Covestro LLC – delivered its reclamation demand to Reichhold within four days of the latter's bankruptcy filing. Covestro later filed a proof of claim in the amount of almost one million dollars, but subsequently amended the proof of claim several times as a result of receiving payments pursuant to a critical vendor agreement. The payments made pursuant to the critical vendor agreement satisfied the section 503(b)(9) portion of Covestro's claim (for goods delivered within 20 days of the petition date) but did not pay its claim in full.

On October 1, 2015, Covestro filed a proof of claim seeking $411,781.72 as an administrative expense. The claim sought the value of goods delivered to the debtor between 21 and 45 days prior to the commencement of the debtor's bankruptcy case. The validity of that claim was challenged by the trustee of the Reichhold Liquidating Trust.

The liquidating trustee asserted that the rights of the lenders under the DIP loan, though they were granted after Covestro's reclamation rights arose, related back to the prepetition lender's rights because the DIP loan repaid the prepetition Oaktree loan. Therefore, the trustee contended that the two liens should

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Reversal, *from page 1*

they would have earned if the notes had not been redeemed early.

"Indentures routinely contain such provisions to protect noteholders against subsequent interest rate drops and the corresponding loss in the bargained-for interest payments should issuers refinance to take advantage of lower cost financings," says Vanessa G. Spiro, a partner at K&L Gates LLP.

The indenture also included an acceleration provision that provided for all outstanding notes to become due immediately if EFH filed for bankruptcy.

When interest rates declined, EFH had good reason to refinance the notes, but doing so outside of bankruptcy would have required it to pay the make-whole premiums. So, the company filed for Chapter 11.

The question before the bankruptcy court, and then the district court, was whether EFH had to pay the make-whole premium given that it was in bankruptcy. Both courts concluded that the company did not. The bankruptcy court noted that "under New York law, an indenture must contain express language requiring payment of a prepayment premium upon acceleration; otherwise, it is not owed."

The district court largely followed the bankruptcy court's analysis, reasoning that the maturity of the notes automatically accelerated upon the commencement of the bankruptcy, and therefore the consideration received by the noteholders under the plan did not constitute a prepayment.

"The courts cited a line of cases that stand for the proposition that where an indenture does not expressly specify that a prepayment premium is owed following automatic acceleration upon a bankruptcy filing, such premium is simply not owed," says Michael H. Goldstein, partner and co-chair of the financial restructuring group at Goodwin Procter LLP. "In addition, the courts found that repayment by a borrower after acceleration cannot, by definition, be voluntary."

According to the Third Circuit, however, filing for bankruptcy does not excuse a debtor from its obligation to pay a make-whole premium due to its lenders.

The court reversed both decisions, holding that EFH was required to pay the make-whole premium. In coming

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Research Report

Who's Who in Key Energy Services, Inc.

by Dave Buzzell

Headquartered in Houston, Texas, Key Energy Services, Inc. (Key), claims to be the largest domestic onshore, rig-based well servicing contractor based on the number of rigs owned.

The company commenced operations in July 1978 under the name National Environmental Group, Inc. In December 1992, the company became Key Energy Group, Inc., changing its name to Key Energy Services, Inc. in December 1998.

Key provides a full range of well services to major oil companies, foreign national oil companies, and independent oil and natural gas production companies. In the first half of 2016, the company's U.S. rig services accounted for over one half of its revenues. These services include the completion of newly-drilled wells, workover and recompletion of existing oil and natural gas wells, well maintenance, and the plugging and abandonment of wells at the end of their useful lives. The company also provide specialty drilling services to oil and natural gas producers and transportation and well-site storage services for various fluids.

Key also offers coiled tubing services and fishing and rental services, which involves recovering lost or stuck equipment in the wellbore utilizing a broad array of "fishing tools."

Key operates in most major oil and natural gas producing regions of the continental United States and also has operations in Canada and Russia. Key's customers include Chevron Texaco Exploration and Production, which accounted for approximately 15% of the company's consolidated revenue in 2016. Key's assets include approximately 880 rigs of various sizes, 2,500 trucks and similar vehicles, and thousands of pieces of other equipment. Key also owns more than 135 pieces of real estate and certain patents and other intellectual property.

On October 24, 2016, Key and three affiliated companies (Misr Key Energy Investments, LLC, Key Energy Services, LLC, and Misr Key Energy Services, LLC) filed petitions in the United States Bankruptcy Court for the District of Delaware seeking relief under Chapter 11. The debtors also filed a joint prepackaged plan of reorganization.

Key blamed its adverse financial condition on a combination of events. Beginning in mid-2014, oil prices began to fall sharply, resulting in a 50% decline over a period of six months, and depressed price conditions persisted and worsened during 2015. In response to declining oil prices, Key's customers substantially reduced their existing production operations and implemented severe cutbacks in capital spending.

As a result, for the year ended December 31, 2015, Key incurred a net loss of $917.70 million on $792.32 million of revenues, compared to a net loss of $178.62 million on $1.42 billion of revenues for the year ended December 31, 2014. As of the second quarter of 2016, Key reported approximately $1.13 billion in total assets and approximately $1 billion in aggregate funded debt.

Under a joint prepackaged plan of reorganization, Key will reduce indebtedness by approximately $725 million, replacing an existing term loan facility with a new term loan facility of $250 million and converting $675 million of senior notes into 100% of key common stock in the reorganized company. Key also plans to replace its existing ABL credit facility with a new ABL credit facility.

Under the joint plan, general unsecured claims are unimpaired and will recover 100%. Platinum Equity, a Los Angeles-based global investment firm, which previously held a majority of Key's senior notes, is now the company's largest shareholder.

On December 6, 2016, the bankruptcy judge confirmed the joint prepackaged plan of reorganization that allowed Key to reduce total indebtedness by over 70% and provide the debtors with long-term financing and access to capital to support ongoing business needs. Key expects to exit bankruptcy with at least $80 million in cash on its balance sheet.

The Debtor

Robert Drummond is president and chief executive officer, **Marshall J. Dodson** is chief financial officer, senior vice president, and treasurer, **David Brunnert** is senior vice president and chief operating officer.

Sidley Austin LLP is serving as counsel. **James F. Conlan** and **Larry J. Nyhan**, co-leaders of the corporate reorganization and bankruptcy group, and **Andrew F. O'Neill**, partner in the firm's Chicago office, and **Jeffrey E. Bjork** and **Christina M. Craige**, partners in the firm's Los Angeles office, lead the engagement.

Young, Conaway, Stargatt & Taylor, LLP is serving as co-counsel, led by partners **Robert S. Brady** and **Edwin J. Harron** and associate **Ryan M. Bartley**.

The investment banker is **PJT Partners LP**, represented by **James Cuminale**, general counsel.

Alvarez and Marsal North America, LLC is serving as financial advisor, with **Edgar W. Mosley**, managing director, leading the engagement.

Deloitte Tax LLP is providing tax advisory and consulting services. **Robert A. Hawkins**, partner, leads the engagement.

Creditors

An official committee of unsecured creditors has not yet been appointed.

Sullivan & Cromwell LLP, led by **Michael H. Torkin**, partner, and **David J. Jakus**, associate, are representing Platinum Equity as well as certain other pre-petition senior noteholders.

Senior noteholders are also being represented by **Cleary Gottlieb Steen & Hamilton LLP**, with **Sean A. O'Neal**, partner, and **Humayun Khalid**, counsel, leading the engagement, and **Morris, Nichols, Arsht & Tunnell LLP**, with partners **Robert J. Dehney**, **Eric D. Schwartz**, **Andrew R. Remming** and associate **Andrew J. Roth-Moore** leading the engagement.

Judge

The judge is the **Honorable Brendan Linehan Shannon**. ¤

Outlook, *from page 2*

Rosenthal: The uncertainty surrounding the impact of Brexit – particularly how it will affect the ability of the U.K. courts to enforce their orders on the continent – may well increase the attractiveness of the United States as the principal filing forum for cross-border cases.

Are there any unexpected areas to watch?

Venditto: An area that has not garnered much attention, but could be ticking economic time bomb, is student loan debt. It is the second largest form of debt in the United States, second only to mortgages, and we all remember how the real estate credit bubble impacted the economy in 2008. According to the U.S. Department of Education, approximately 44 million Americans collectively owe more than $1.3 trillion in student loans and more than 40 percent of student loan borrowers are either in default, delinquency, or have postponed repaying their student loans. But these statistics do not fully explain the actual impact of this debt. Surveys indicate that this debt has caused many of the borrowers to delay doing some of the things that drive

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Reclamation, *from page 2*

be viewed as an "integrated transaction." Moreover, he argued that Covestro's rights were extinguished when Reichhold repaid the prepetition loan because reclamation permits a seller to reclaim only the goods themselves and Covestro's goods were used to repay the prepetition lender.

The liquidating trustee's position was based upon precedent from the Southern District of New York bankruptcy court. First, a 2003 decision arising out of the bankruptcy case of *Dairy Mart Convenience Stores, Inc.* held, according to Judge Walrath, that "where a prepetition secured lender had a floating lien on inventory and was paid from the proceeds of a post-petition loan supported by a new floating lien, the goods securing the prepetition lender's debt were effectively used to repay that debt." Similarly, the court in that case related the postpetition lien back to the prepetition lien, finding both liens were an "integrated transaction," notwithstanding that the postpetition lien was granted after the reclamation rights arose.

A second decision, this time arising out of *Dana Corp.'s* bankruptcy case, followed the same line of reasoning. Therein, the court allowed a similar relation back, stating that "[b]ecause the reclaimed goods or the proceeds thereof were either liquidated in satisfaction of the Prepetition Indebtedness or pledged to the DIP Lenders pursuant to the DIP Facility, the reclaimed goods effectively were disposed of as part of the March 2006 repayment of the Prepetition Credit Facility." Therefore, the court held that the reclamation claims were valueless.

Covestro relied upon a 2008 decision by the Sixth Circuit Court of Appeals in opposing the liquidating trustee's objection to its reclamation claim. In that decision, which arose from the *Phar-Mor* bankruptcy case filed in the Northern District of Ohio bankruptcy court, the Sixth Circuit expressly considered and rejected the earlier Southern District of New York decisions in *Dairy Mart* and *Dana Corp*. Instead, the Sixth Circuit affirmed the Ohio bankruptcy court's decision that a postpetition lender's floating lien on the debtor's inventory did not constitute an assumption of the prepetition creditor's lien, but an entirely new lien that did not defeat an intervening reclaiming seller's rights.

Judge Walrath agreed with the Sixth Circuit's ruling in *Phar-Mor*, stating that she found it "too much of a stretch to conclude, as the *Dairy Mart* and *Dana Corp.* courts did, that the repayment of the Prepetition Loan from the DIP Loan was repayment from the 'sale' of the reclaiming creditor's goods." Rather, she emphasized that Covestro's goods were not sold, nor were their proceeds paid to the prepetition lender. "In this case, when the Prepetition Loan was paid from the DIP Loan, the Prepetition Lender's lien was satisfied but Covestro's reclamation rights remained in force," she wrote. "The fact that funds obtained from the DIP Loan were used to satisfy the Prepetition Loan, or that the Debtor granted the DIP Lenders a lien in inventory to obtain such funds, is irrelevant. Covestro's reclamation rights arose before the DIP Lenders' security interest attached, and the DIP Lenders' lien was expressly subject to reclamation rights under section 546."

Judge Walrath similarly rejected the liquidating trustee's "integrated transaction" argument. Rather, she stressed that the prepetition loan and the DIP loan "were two different loans by two different lenders at two different times." Therefore, she

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Calendar

American Bankruptcy Institute
2017 Caribbean Insolvency Symposium
February 9 – 11, 2017
Westin Grand Cayman
Grand Cayman, Cayman Islands
Contact: www.abi.org

American Bankruptcy Institute
VALCON 2017
March 1 – 3, 2017
Four Seasons Hotel Las Vegas
Las Vegas, NV
Contact: www.abi.org

National Association of Bankruptcy Trustees
2017 Spring Seminar
March 1 – 5, 2017
The Gran Melia Resort
Rio Grande, Puerto Rico
Contact: www.nabt.com

INSOL International
Tenth World Quadrennial Congress
March 19 – 22, 2017
International Convention Centre
Sydney, Australia
Contact: www.insol.org

Turnaround Management Association
TMA MidAmerica Regional Conference
April 5 – 7, 2017
MGM
Detroit, MI
Contact: www.turnaround.org

American Bankruptcy Institute
2017 Annual Spring Meeting
April 20 – 23, 2017
Marriott Marquis
Washington, DC
Contact: www.abiworld.org

Association of Insolvency & Restructuring Advisors
33rd Annual Bankruptcy & Restructuring Conference
June 7 – 10, 2017
Four Seasons Resort & Club
Dallas, TX
www.aira.org ¤

Special Report

Largest Bankruptcy Filings – 2016

Company Name	Industry	Filing Information	Assets	Debtor's Counsel
SunEdison	Manufacturing	Filed: April 21, 2016 New York, Southern Judge Stuart Bernstein	$20,700,000,000	Jay Goffman, Eric Ivester Skadden, Arps, Slate, Meagher & Flom New York, NY
Linn Energy	Mining	Filed: May 11, 2016 Texas, Southern Judge David Jone	$11,610,000,000	Paul Basta, Stephen Hessler Kirkland & Ellis New York, NY
Peabody Energy	Mining	Filed: April 13, 2016 Missouri, Eastern Judge Barry Schermer	$11,020,000,000	Heather Lennox, Amy Edgy Jones Day Cleveland, OH
SandRidge Energy	Mining	Filed: May 16, 2016 Texas, Southern Judge David Jones	$7,010,000,000	James Sprayregen Kirkland & Ellis Chicago, IL
Arch Coal	Mining	Filed: January 11, 2016 Missouri, Eastern Judge Charles Rendlen	$5,840,000,000	Brian Walsh Bryan Cave Dallas, TX
BreitBurn Energy Partners	Mining	Filed: May 15, 2016 New York, Southern Judge Stuart Bernstein	$4,700,000,000	Ray Schrock, Stephen Karotkin Weil Gotshal & Manges New York, NY
Republic Airways Holdings	Transportation & Warehousing	Filed: February 25, 2016 New York, Southern Judge Sean Lane	$3,560,000,000	Bruce Zirinsky, Sharon Richardson Zirinsky Law Partners New York, NY
Verso Paper Holdings	Manufacturing	Filed: January 26, 2016 Delaware Judge Kevin Gross	$2,900,000,000	Gregory Davis, Peter Friedman O'Melveny & Myers New York, NY
Halcon Resources Corp.	Mining	Filed: July 27, 2016 Delaware Judge Brendan Linehan Shannon	$2,840,000,000	Gary Holtzer, Joseph Smolinsky Weil, Gotshal & Manges New York, NY
Paragon Offshore	Mining	Date Filed: February 15, 2016 Delaware Judge Christopher Sontchi	$2,470,000,000	Gary Holtzer, Stephen Youngman Weil, Gotshal & Manges New York, NY
CHC Group	Transportation & Warehousing	Filed: May 5, 2016 Texas, Northern Judge Stacey Jernigan	$2,160,000,000	Stephen Youngman, Gary Holtzer Weil, Gotshal & Manges Houston, TX
Roust Corporation	Manufacturing	Filed: December 30, 2016 New York, Southern Judge Robert Drain	$1,980,000,000	Jay Goffman, Mark McDermott Skadden, Arps, Slate, Meagher & Flom New York, NY
RCS Capital Corporation	Finance & Insurance	Filed: January 31, 2016 Delaware Judge Mary Walrath	$1,970,000,000	Michael J. Sage, Shmuel Vasser Dechert New York, NY
Seventy Seven Energy	Mining	Filed: June 7, 2016 Delaware Judge Laurie Selber Silverstein	$1,770,000,000	Emanuel Grillo, Christopher Newcomb Baker Botts New York, NY
Sports Authority	Retail Trade	Filed: March 2, 2016 Delaware Judge Mary Walrath	$1,600,000,000	Robert Klyman, Michael Williams Gibson, Dunn & Crutcher Los Angeles, CA
Atlas Resource Partners	Mining	Filed: July 27, 2016 New York, Southern Judge Sean Lane	$1,320,000,000	David Turetsky, Ron Meisler Skadden, Arps, Slate, Meagher & Flom New York, NY

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Worth Reading

The Turnaround Manager's Handbook

Author: Richard S. Sloma
Publisher: Beard Books
Softcover: 242 pages
List Price: $34.95

In the introduction to this book, the author suggests that an accurate subtitle could be "How to Become a Successful Company Doctor." Using everyday medical analogies throughout, he targets "corporate general practitioners" charged with the fiscal health of their companies.

As with many human diseases, early detection of turnaround situations is critical. The author describes turnaround situations as a continuum differentiated by length of time to disaster: "Cash Crunch," "Cash Shortfall," "Quantity of Profit," and "Quality of Profit."

The book centers on 13 steps to a successful turnaround. Extensive data collection and analysis are required, including the quantification of 28 symptoms, the use of 48 diagnostic and analytical tools, and up to 31 remedial actions.

The first step is to determine which of 28 symptoms are plaguing the company. The symptoms generally pertain to manufacturing firms, but can be applied to service or retail companies as well. Most of the symptoms should be familiar to the reader, but Sloma lays them out systematically and relates them to the analytical tools and remedial actions found in subsequent chapters. The first seven involve the inability to make various payments, from debt service to purchase commitments. Others include excessive debt/equity ratio, eroding gross margin, increasing unit overhead expenses, decreasing product line profitability, decreasing unit sales, and decreasing customer profitability.

Step 2 employs 48 diagnostic and analytical tools to derive inferences from the symptom data and to judge the effectiveness of any proposed remedy. Says the author, "If the only tool you have is a hammer, you will view every problem only as a nail!" He then proceeds to lay out all 48 tools in his medical bag, which he sorts into two kinds: macro tools and micro tools. Macro tools require data from several symptoms or are used to assess and evaluate more than a single symptom, whereas micro tools are more general purpose in function. The 12 macro tools run from "The Art of Approximation" to "Forward-Aged Margin Dollar Content in Order Backlog." The 36 micro tools include "Product Line Gross Margin Percent Profitability;" "Finance/Administration People Related Expenses as Percent of Sales," and "Cumulative Gross $ by Region."

Next, managers are directed to 31 possible remedial actions. The first six actions are to be considered at the Cash Crunch stage, and range from a fire sale of inventory to factoring accounts receivable. The next six deal with reducing people-related expenses, followed by 13 actions aimed at reducing product- and plant-related expenses. The subsequent five actions include eliminating unprofitable products, customers, channels, regions, and reps. Finally, managers are advised on increasing sales and improving gross margin by cost reduction in various ways.

The remaining steps involve devising the actual turnaround plan, ensuring management and employee ownership of the plan, and implementing and monitoring the plan. The advice is comprehensive, sensible, and encouraging, but doesn't stoop to cliche or empty motivational babble. The author has clearly operated on patients before, and his therapeutics have no doubt restored many a firm to financial health. ¤

Richard Sloma, an internationally acclaimed lecturer, has decades of experience as a board member, chairman, chief executive officer, and chief operating officer.

This book may be ordered by calling 888-563-4573 or by visiting www.beardbooks.com.

Outlook, *from page 4*

the economy, such as purchasing a car or home or saving for retirement. Even if this debt load does not itself disrupt the economy, it will be a significant drag on economic growth in coming years.

Which bankruptcies will likely be resolved?

Feder: 2017 will see the end of three of the largest and most complicated cases ever – Nortel, Energy Future Holdings, and Caesars.

Which sectors will see activity or challenges?

Charleston: Our firm believes the U.S. oil and gas industry is expected to continue to generate several distressed investment opportunities in 2017, as low oil prices are expected to create cash-flow problems, and access to sources of funding for these companies is likely to remain limited in 2017. The metals and mining sector is expected to have the highest default rate in 2017, primarily due to low metal prices. Brick-and-mortar retailers will likely continue to flounder.

What will be your greatest challenge in 2017?

Feder: As always, adapting to a rapidly changing economic environment and anticipating where opportunities will lie.

Venditto: The risk of trade and currency wars. After the Trump administration takes office in January, we expect to see some significant policy changes, the nature and extent of which are unknown. Identifying and adapting to their economic impact will be the biggest challenge in the new year. If the new administration is able to implement some of the policies advocated in campaign rhetoric, we may see significant tax cuts and increased government spending on infrastructure and defense programs. This may stimulate the economy in the near term, but increase the federal deficit. Growth will be tempered by higher interest rates and the difficulty of growing an economy that is near statistical full employment. The big unknown, however, will be how the new administration changes trade policy. A more protectionist approach will impact U.S. businesses in different ways. While some may benefit, others will be hurt if retaliatory policies are implemented by key trading partners. ¤

Special Report

Successful Restructurings – 2016, page 1

Aéropostale

Restructuring Firm: FTI Consulting (Gina Gutzeit)

Investment Banking Firm: Stifel Financial Corp. (Michael J. Kollender)

Counsel to Debtor: Weil, Gotshal & Manges (Ray Schrock, Michael Aiello, Jacqueline Marcus, Garrett Fail, Gavin Westerman)

One of the year's highest-profile bankruptcies, Aéropostale filed for chapter 11 amidst mounting pressure to liquidate. The company faced numerous difficulties, ranging from uncooperative pre-petition ABL lenders, ongoing litigation with term loan lenders, a weak retail and mall environment, and poor historical financial performance. Aéropostale rewrote the 363 playbook by orchestrating a going-concern sale to a first-of-its-kind buyer consortium that included the retailer's major landlords and a brand management company. Given the company's contentious restructuring, reaching a consensual agreement amongst all stakeholders while keeping the majority of stores open was a major accomplishment. The going-concern sale helped preserve more than 500 stores and nearly 13,500 employees. The sale also protected Aéropostale's suppliers that had exposure to purchase orders of over $250 million for the upcoming holiday season.

Alphatec

Restructuring Firm: Gordian Group (Peter Kaufman, Henry Owsley, David Herman, Patricia Caldwell, Dennis McGettigan, Fred Zeidman)

Counsel to Debtor: Latham & Watkins (Matt Bush)

Alphatec, a publicly-traded medical technology company focused on spinal fusion technologies, had seen its revenue and margins drop as a result of an in-process restructuring of its distribution channels. At the same time, the company had been forced to tap a high-coupon loan to fund a litigation settlement. The company and its advisors pursued a strategy whereby Alphatec sold its international operations for $80 million to Globus Medical,which provided Alphatec a term loan to fund the restructuring of its U.S. operations. Proceeds from the transaction were used to right-size the company's balance sheet and fund capital expenditures necessary to renew growth in Alphatec's U.S. operations. Absent a transaction, Alphatec would have run out of cash and have had to file for bankruptcy protection, wiping out shareholders in the process.

Arch Coal

Restructuring Firm: PJT Partners (Mark Buschmann)

Counsel to Debtor: Davis Polk & Wardwell (Marshall S. Huebner, Brian M. Resnick)

The restructuring of Arch Coal and its 71 wholly-owned domestic subsidiaries is considered one of the great restructuring stories in an industry beset by years of reduced demand, declining prices, and increased regulation. With a confirmed plan in just eight months, the case is possibly the fastest multibillion dollar non-prepackaged bankruptcy in any industry in recent memory. The case began from an adversarial posture and could well have fallen into protracted litigation. However, in just seven months Arch achieved a global settlement that paved the way to an expedited confirmation to which no economic stakeholder objected. The notably successful and efficient restructuring ultimately obtained the support of 100% of prepetition first lien term loan lenders and 98% of prepetition second lien and senior unsecured noteholders and eliminated more than $4.5 billion of debt from the company's balance sheet.

Atlas Resource Partners

Counsel to the Partnership: Skadden, Arps, Slate, Meagher & Flom (Ron E. Meisler, Felicia Gerber Perlman, David M. Turetsky)

Financial Advisor: Perella Weinberg Partners (Kevin M. Cofsky)

A master-limited partnership, Atlas Resource Partners (ARP) received court approval for its prepackaged restructuring and successfully emerged as Titan Energy a month after filing for Chapter 11. As master limited partnership, ARP was treated as a partnership for U.S. federal income tax purposes, meaning that all items of income, gain, deduction, and loss were passed through to ARP's unitholders. ARP therefore faced tax-related challenges regarding the recognition of cancellation of debt income (CODI) in a restructuring. ARP utilized an innovative structure to mitigate the CODI that would be recognized by ARP's stakeholders, and successfully executed the first ever prepackaged restructuring of a publicly traded master-limited partnership. The restructuring reduced Atlas' debt by approximately $900 million and interest expenses by $80 million per year.

Binder & Binder – The National Social Security Disability Advocates

Restructuring Firm: Development Specialists, Inc. (William A. Brandt, Jr., Fred C. Caruso, Patrick J. O'Malley, Joseph J. Luzinski, Yale S. Bogen, Shelly L. Cuff)

Counsel to Debtor: Lowenstein Sandler (Kenneth A. Rosen, Mary E. Seymour, Andrew D. Behlmann, Nicholas B. Vislocky)

Binder & Binder represented claimants in more than 57,000 Social Security and Veterans Administration disability cases and employed nearly 1,000 employees in 35 offices across the country. Any interruption in the company's operations would have delayed clients' receipt of much-needed benefits when such a delay could prove catastrophic. Through skillful deal making with the company's labor unions, key employees, lenders, creditors, and other major constituencies, as well as through strategic litigation, the company was able to right-size its operations, stabilize cash flow, maximize value for creditors, preserve hundreds of jobs, and ultimately obtain confirmation of a unique Chapter 11 plan that provided for a unique hybrid reorganization in which the debtors reorganized and continued representing existing clients while the company's founders purchased its intellectual property and have begun taking new cases.

C&J Energy Services Ltd.

Restructuring Firm: AlixPartners (Rebecca A. Roof, Carrianne Basler)

Counsel to Debtor: Kirkland & Ellis (James H.M. Sprayregen, Marc Kieselstein, Chad J. Husnick, Emily E. Geier)

Counsel to Unsecured Creditors: Greenberg Traurig (David B. Kurzweil, Shari L. Heyen, Lenard M. Parkins, Karl D. Burrer, David R. Eastlake)

One of the largest, integrated oilfield services companies in North America, C&J Energy suffered not only the unexpected loss of its CEO and founder, but also a prolonged downturn in the energy exploration and production space that had a significant impact on the company and its customers. Despite numerous challenges from a majority shareholder, the company was able to successfully negotiate a consensual resolution with the holders of $1.4 billion in prepetition secured indebtedness and successfully emerge in less than 6 months. The plan resulted in a total deleveraging of its balance sheet. Among other things, the plan established a liquidating trust funded with at least $33 million in cash and valuable new warrants. Recoveries for unsecured creditors could be in excess of 90% after exercising the warrants.

Special Report

Successful Restructurings – 2016, page 2

Energy XXI

Restructuring Firm: Opportune (David Baggett)
Investment Banking Firm: PJT Partners (Tim Coleman, Peter Laurinaitis, Adam Pilchman)
Counsel to Debtor: Vinson & Elkins (Harry Perrin, David Meyer, Jessica Peet, Lauren Kanzer)

The largest independent offshore operator, Energy XXI was the first to successfully reorganize its balance sheet in the recent wave of oil and gas restructurings – a noteworthy accomplishment given the unique challenges such companies face in reorganizing and the low probability of success similarly situated companies have historically achieved in Chapter 11. Although the company entered Chapter 11 with a restructuring support agreement that implemented a complex deleveraging, rebounding oil prices galvanized unsecured noteholders to organize, resulting in increasingly litigious Chapter 11 cases with high stakes at play. Through significant negotiation and mediation, a fully consensual plan was reached that eliminated more than $3.6 billion of debt, giving the company enhanced flexibility to operate in the new oil and gas pricing environment and weather the challenges facing the offshore exploration and production industry.

Quiksilver

Restructuring Advisor: FTI Consulting
Investment Banker: Peter J. Solomon Company
Counsel to Debtor: Skadden, Arps, Slate, Meagher & Flom (Van C. Durrer II)

A manufacturer of sporting goods and apparel, Quiksilver and its wholly owned subsidiary, Boardriders S.A. (Luxembourg), commenced a global restructuring process, including filing for Chapter 11 protection for its U.S. entities. The reorganization involved over half a billion dollars in debt – the largest Chapter 11 reorganization of a retailer in over 10 years – and ended with all off-shore creditors receiving a 100% recovery. The restructuring plan was initially opposed by unsecured creditors, but an agreement was reached allowing unsecured bondholders to take an increased 4.75% stake in Quiksilver, thus allowing more cash to flow to other unsecured creditors not concerned with holding equity. With the deal, the parties were able to avoid a highly contentious valuation trial for which the court had booked three full days.

RCS Capital Corporation and subsidiaries (including Cetera Financial Group, n/k/a Aretec Group, Inc.)

Investment Banking Firm: Lazard Freres & Co. (Andrew T. Yearley)
Counsel to Debtor: Dechert (Michael J. Sage, Shmuel Vasser)
Counsel to RCS Creditors' Committee: Gibson Dunn (David Feldman)

RCS Capital is the second-largest independent financial advice network in the United States. After several major acquisitions, the company's funded indebtedness had reached more than $873 million leading it to seek Chapter 11 protection. The restructuring posed a number of unique challenges, including avoiding regulatory action against the broker-dealers, avoiding filing the advisory business so as to maintain its client base and minimize advisor attrition, and releasing all RCS entities from their direct or guaranty liability for the funded debt. A novel, dual-step restructuring strategy was formulated that helped the company reduce its debt by $500 million, solidify long-term growth, and secure liquidity. The company accomplished this within a four-month Chapter 11 timeframe and emerged without the unplanned loss of independent investment advisors or clients, a substantial achievement given the nature of the industry concerned.

Sabine Oil & Gas

Restructuring Firm: Lazard (Brandon Aebersold, Parry Sorenson)
Restructuring Firm: Zolfo Cooper (Joff Mitchell, Jesse Delconte, Andrew Ralph)
Counsel to Debtor: Kirkland & Ellis (Jonathan Henes, Christopher Marcus, Ryan Bennett, Gabor Balassa, Katie Jakola)

After more than a year of litigation (in the context of multiple motions for derivative standing and confirmation of its Chapter 11 plan) Sabine Oil & Gas – an independent oil and gas exploration and production company with approximately $2.6 billion in outstanding funded debt obligations – confirmed a plan of reorganization that significantly reduced its debt obligations and secured the financial commitments necessary to fund the restructuring and go-forward business needs. In addition, Sabine successfully obtained the bankruptcy court approval needed to reject certain onerous midstream gas gathering agreements and better position the business for post-emergence success. The case had numerous innovative components including a likely precedent-setting victory for Sabine on a previously untested matter of law involving the rights of bankrupt "upstream" oil and gas producers and their "midstream" contract counterparties.

Verso Corporation

Restructuring Firm: PJT Partners (Steve Zelin, Andrew Pilchman)
Restructuring Firm: Alvarez & Marsal (Dennis Stogsdill, Victor Chemtob, Nick Campbell, Jeff Sielinski)
Counsel to Debtor: O'Melveny & Myers (George Davis, Andrew Parlen, Peter Friedman, Suzzanne Uhland, Daniel Shamah)

Verso's filing was one of the largest and most complex of 2016. The complexity stems from the merger between Verso and NewPage Corporation, which closed a year earlier. Even though Verso and NewPage merged into one business, in many ways their full integration was not complete, including separate capital structures, with over $2.8 billion of debt owed to different constituencies with separate liens and security interests. Further, technological changes on the demand for paper and pulp resulted in NewPage filing for Chapter 11 protection twice in less than 5 years, creating an agitated and skeptical community of creditors. Also, the existence of separate secured lender groups bred an intricate predicament in reaching a consensual restructuring agreement with all parties. Despite these burdens, Verso emerged from Chapter 11 in less than 6 months without any material legal battles.

Walter Energy

Financial Advisor: AlixPartners (James A. Mesterharm, Joseph Mazzotti, Pilar Tarry)
Counsel to Debtor: Paul, Weiss, Rifkind, Wharton & Garrison (Stephen J. Shimshak, Kelley A. Cornish, Claudia R. Tobler, Ann K. Young, Michael S. Rudnick)
Counsel to Informal Group of Senior Secured Lenders and Noteholders: Akin Gump (Ira Dizengoff, James Savin, Lisa Beckerman)

A leading producer and exporter of metallurgical coal for the global steel industry, Walter Energy's restructuring was one of the heavyweight events of 2016, totaling more than $3 billion in debt. Negotiations involved separating core assets and non-core assets, which allowed the company to sell core assets free and clear to senior secured lenders and noteholders. In connection with the sale, the company and lenders successfully prosecuted over vigorous objection motions, among other things, terminating existing union collective bargaining agreements and allowing withdrawal from a significantly underfunded multi-employer pension plan. By unburdening the company's productive assets from massive legacy liabilities, the restructuring successfully preserved and enhanced the ongoing business, saved employees' jobs, and maximized recoveries to creditors. ¤

Reclamation, *from page 4*

determined that Covestro's rights arose first and the DIP lenders did not have prior rights in the goods under section 546(c).

Several industry observers note that Judge Walrath's decision may give reclamation claimants additional hope, but will also require diligence in protecting their rights. "A seller should not necessarily count out reclamation rights when seeking to protect its interests in a debtor-buyer's bankruptcy proceedings," says Kayla Henderson of Robison, Curphey & O'Connell. "The seller should watch the buyer's case carefully, and if the prepetition lender to the buyer is paid and its lien extinguished, the seller's reclamation claim may have a chance to defeat a DIP lender's post-petition lien." Foley's Jill Nicholson notes that reclamation claimants may need to be active from the beginning of cases to avoid having their rights compromised. "While assessing options and seeking to reduce risk, credit managers will want to closely review the debtor's proposed financing arrangements to determine (a) if the post-petition lender will be granted a lien on the debtor's inventory and (b) whether there is a provision stating that the new loan is subject to liens perfected after bankruptcy under section 546(b)," Nicholson notes. "If the proposed DIP loan lacks such a provision, credit managers should consider participating early in the case and objecting to financing orders that do not allow for reclamation or provide a carve-out from the DIP lender's collateral to secure payment of these claims." ¤

Reversal, *from page 2*

to that decision, the court asked two questions. First, was there a redemption? Second, if there was a redemption, was the redemption optional?

In regard to the first question, the Third Circuit relied on rulings of New York and federal courts to conclude that the term "redemption" encompasses both pre- and post-maturity repayments of debt.

In regard to the second question, the court did find the redemption to be optional because EFH voluntarily filed for Chapter 11 protection intending to refinance the notes – a refinancing that was being undertaken to cut its interest expense, which is the very reason make-whole provisions exist. It had also repaid the notes over the noteholders' objections.

The Third Circuit also reviewed the make-whole provision and the acceleration provision in the indentures and did not find them inconsistent. Nothing in the acceleration provision, it said, negated the make-whole premium. If an optional redemption occurred prior to the stated date, the make-whole payment was due.

The opinion makes it clear that the burden is on borrowers to make explicit in their loan agreements whether an acceleration provision is intended to override an optional redemption provision.

"The Third Circuit Court of Appeals' ruling was fact-specific and focused on the particular circumstances present in the indentures at issue," say Rudolph J. Di Massa, Jr., a senior partner at Duane Morris LLP and chair of the firm's business reorganization and financial restructuring group, and Drew S. McGehrin, an associate at Duane Morris. "The majority of the Third Circuit Court's opinion discussed the particular language of the indenture provisions governing acceleration and the make-whole premiums. The Third Circuit Court therefore delivered a decision that was focused on the particular facts of the case rather than hand down precedent that may affect similar contracts without regard to specific contract terms. "

Keeping this in mind, however, Di Massa and McGehrin say attorneys drafting provisions like these are now aware of the need for precision and clarity as to the viability and applicability of similar provisions, especially with regard to situations of possible redemption. Other attorneys agree.

"The precise language regarding the circumstances under which these payments become due matters significantly," says Spiro. "Clear language in debt documentation providing for the payment of make-whole amounts after acceleration or upon 'redemption' prior to a date certain is critical in demonstrating the parties' intent that make-whole amounts are due if the debt is repaid after acceleration."

"Regardless of whether the Third Circuit's ruling in Energy Future is the right one, the decision emphasizes, once again, that precise drafting is critical," says Goldstein. "If the objective of the parties is for no prepayment premium to be charged in the event of automatic acceleration or other remedy following an event of default (bankruptcy or otherwise), best practices recommend that the indenture should explicitly state that the prepayment premium is not triggered in such circumstances."

"As long as the parties (through counsel) make their intentions clear at the outset, they will probably be able to avoid the litigation that resulted in the EFH matter," add Di Massa and McGehrin.

It is noteworthy that the Third Circuit's decision is a departure from other recent make-whole decisions. For example, the court disagreed with the New York bankruptcy and district courts' holdings in the Momentive bankruptcy cases. On December 15, Energy Future Holdings asked the Third Circuit to reconsider and to remand the case to the New York Court of Appeals and, according to Di Massa and McGehrin, this may be an attempt to obtain more time in awaiting the Second Circuit Court of Appeals' pending decision in *Momentive*.

"In *Momentive*, the Second Circuit Court of Appeals is reviewing New York bankruptcy and district court rulings on language in certain indentures that was very similar to the language at issue in one of the indentures in the EFH case," say Di Massa and McGehrin. "The *Momentive* case has followed the same path as EFH: the bankruptcy and district courts in both cases held that the make-whole premiums were not due under the language of the indentures."

continued on page 11

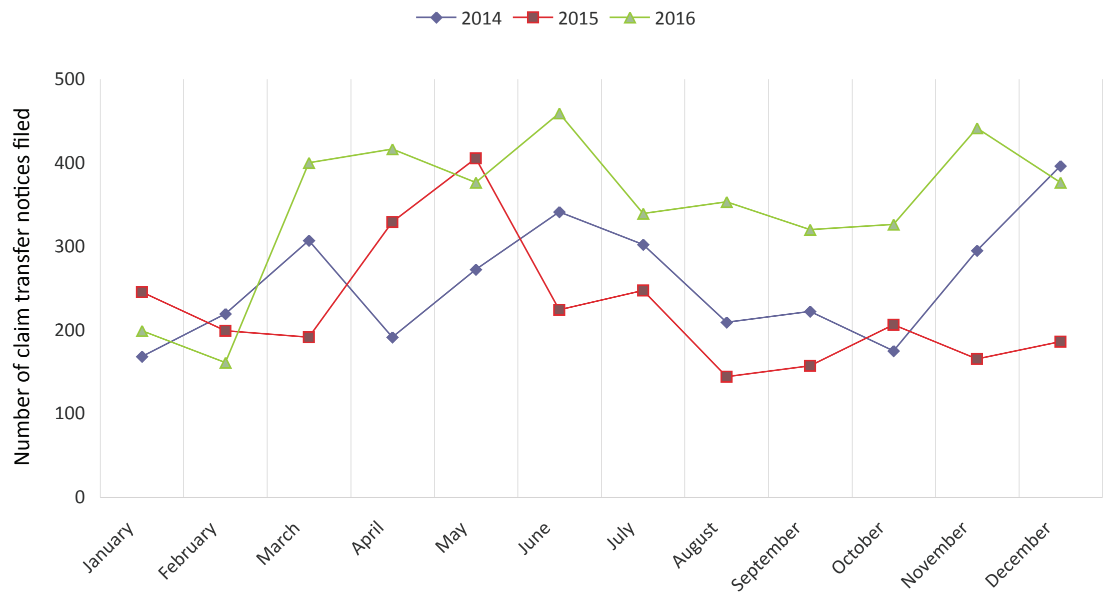
Special Report

Claims Trading Activity

The following charts reflect our analysis of over 17,500 notices of claim transfers filed in large Chapter 11 bankruptcy cases nationwide from January 1, 2014 to December 31, 2016. The court filings were aggregated from a review of court dockets across more than 2,300 cases. A list of the cases covered by our analysis can be found here: https://www.chapter11dockets.com/about/cases.

CHAPTER 11 DOCKETS

Excluding Lehman Bros., Claims Trading Activity Was Robust in 2016 Relative to the Previous Two Years



Most Active Bankruptcy Cases for Claims Trading Activity in 2016

By Asserted Amount of Claims Transferred

Lehman Brothers Holdings Inc.

Palmdale Hills Property, LLC

Ultra Petroleum Corp.

Republic Airways Holdings Inc.

SH 130 Concession Company, LLC

Peabody Energy Corporation

Horsehead Holding Corp. (2016)

Life Partners Holdings, Inc.

Emerald Oil, Inc.

CHC Group Ltd.

Most Active Bankruptcy Cases for Claims Trading Activity in 2016

By Number of Claim Transfer Notices Filed

Lehman Brothers Holdings Inc.

Life Partners Holdings, Inc.

Caesars Entertainment Operating Company, Inc.

Energy XXI Ltd.

Victory Medical Center Mid-Cities, LP

Alpha Natural Resources, Inc.

Ultra Petroleum Corp.

CJ Holding Co.

Horsehead Holding Corp. (2016)

Nortel Networks Inc.

¤

Gnome de Plume

What Will 2017 Bring?

by Deborah Hicks Midanek

It is sobering to be invited to offer an outlook for the year ahead. This year, as we welcome a new President who is no stranger to the restructuring community, we all know that, while we know what we know, we know that what we know may not be true. Similar to the sentiments expressed by Donald Rumsfeld years ago, knowing what we don't know may not offer any comfort either, as perception and reality have to a great extent merged, and we really cannot distinguish between what we know we don't know and what we don't know we don't know.

We face unprecedented uncertainty, not so much as a function of our unpredictable President-elect, but because we have trouble discerning among factual information, or what we know; lack of information, or what we don't know; and misinformation and disinformation, or what we don't know we don't know. The information we receive is often immediate and disseminated as is, making it difficult for us to assess what is being said.

Objective reporting appears no longer to be something establishment media even pretend to try for, and we have no filters to enable assessment of the accuracy of the myriad independent sources of information out there. And, to that mix should be added widespread ignorance and apathy as well as the friction among countrymen being stirred up as we live through the digital revolution – a revolution more profound than the industrial revolution. The entire country, it seems, is at the mercy of its emotions. While this is hardly unique, both scale and stakes are very high.

Thus, this year I feel I have license to predict whatever I imagine, with impunity. And I do offer some predictions, but not about the traditional cycle of which industries are up and which will be down. We in the restructuring community have long been accustomed to a linear world where low interest rates indicate low volume of work for us, so we have been busy lowering our golf handicaps, writing books, and taking up watercolors. 2016 brought some of us off the benches and into the trenches and the swagger was back. Are we now at the broader watershed the industry has been pining for?

As Trump trumps and Putin puts it to us, we are forced to confront the damage hackers can do. Is the DNC, the RNC, or both, now creatures of Russia? The combination of political and economic uncertainty with growing cyber espionage offers a potent mix for us old-fashioned restructuring folks accustomed to worrying about interest rates, covenants, and cash flow. When Wikileaks carries more credibility than the *New York Times,* and when Presidential candidates are not assumed to be truthful or even patriotic, the environment we are operating in is peculiar, to say the least.

Here is my prediction: that the skills required to successfully navigate the zero-sum game environment of a complex bankruptcy, sift imperfect information in a contentious situation and determine which data are important and actionable, and maintain a skeptical frame of mind while moving all parties forward to resolution are exactly the skills required to successfully navigate the brave new world we enter on January 20.

As folks accustomed to operating in gray areas seeking true north in difficult circumstances, we thus bear a heavier-than-average responsibility for keeping our nation safe. While hardly the full employment act for restructuring professionals that we have been awaiting, those of us prepared to step up for what may be a very different set of battles than we have ever faced should turn our phones on again and pay attention. ¤

Ms. Midanek is President of Solon Group, Inc. and can be reached at dhmidanek@solongroup.com.

Reversal, *from page 9*

Consequently, Di Massa and McGehrin note, the EFH debtors may be hoping for one of two results. First, that the Third Circuit Court of Appeals certifies the "make-whole" question to the New York Court of Appeals because the contracts in EFH were to be interpreted under New York law (and were the Third Circuit Court of Appeals to do so, EFH would effectively get a "second bite at the apple" and be permitted to re-argue the issues on which it was unsuccessful before the Third Circuit Court). Second, that even if the Third Circuit Court of Appeals were to eventually deny the motion for reconsideration or certification, the reconsideration process buys enough time to allow the Second Circuit Court of Appeals to affirm the lower courts' decisions in *Momentive*, thereby creating a circuit split on the issue.

"If this were to occur, EFH could have grounds to proceed with a petition for writ of certiorari to the Supreme Court," predict Di Massa and McGehrin. ¤

In the Next Issue…

- *Special Report: Nation's Largest Industrial Auctioneers*
- *Special Report: Major Financial Advisors*
- *Research Report: Who's Who in Performance Sports Group, Ltd.*

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