



AMERICAN
BANKRUPTCY
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2019 Southwest Bankruptcy Conference

ABI Talks

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Pachulski Stang Ziehl & Jones LLP; San Francisco

Divisive Mergers

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Retail Bankruptcies: Where We've Been and Where We're Going

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O'Melveny & Myers LLP; San Francisco

Derivatives in Bankruptcy: The Basics

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Davis Polk & Wardwell LLP; New York

New UST Fees and Their Potential Impact

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Donlin, Recano & Company, Inc.; New York

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American Bankruptcy Institute Southwest Bankruptcy Conference, 2019 ABI Talks

- I. Introduction.
 - A. Introduce myself.
 - B. A brief overview of Divisive Mergers- a corporate oxymoron.
- II. What is a divisive merger?
 - A. Corporate mitosis.
 - 1. For those that remember their High School biology, cellular mitosis is the process wherein one cell reproduces by splitting itself into two cells.
 - B. Divisive merger is a statutory (in some jurisdictions) process that allows a corporate entity to divide itself into two or more separate and distinct entities, with a few key features:
 - 1. Transfers are deemed not transfers.
 - a. No 3rd party consent required (such as lease).
 - b. No transfer taxes.
 - 2. Liabilities can be bindingly allocated.
- III. A few of the jurisdictions that have a form of division statute:
 - A. Delaware, Texas, Arizona and Pennsylvania.
- IV. Potential Bankruptcy Implications.
 - A. If a transfer is statutorily deemed not a transfer, is it avoidable under §§ 544, 547, 548.
 - B. Perfection Issues-Division Company has assets but UUC-1 name of Surviving Company.
 - C. Can it be used in a Plan adverse to creditors?

ABI Outline

Retail: Where we've been, where we're going

I. A brief (recent) history of retail bks:

Late 80's early 90's

- Retail companies were LBO targets because of cash generating ability
- Chapter 11 filings driven by the need to address capital structure / interest rates
- Many retailers operated for more than a year in chapter 11 - enabling company to do a store-by-store analysis over a complete selling season to pick best performing stores
- Typical cap structure included secured bank debt, unsecured bond debt and unsecured trade debt
- Many retailers successfully reorganized (e.g. Macy's)

Early 2000's

- Retail chains suffering from "big Box" retailers
- BAP CPA enacted in 2005 - placed limit on time to assume or reject leases
- Most retailers forced to pursue a sale strategy
- Start to see transactions where a liquidation may yield more value
 - Lease "designation rights"
 - IP rights
 - Liquidation of inventory

Today:

- Retail chains face pressure from “Amazon Effect”
- Impacting both “brick and mortar” and online businesses
- Some businesses (such as grocery chains) face sale pressure in light of real estate footprint
- But landlords growing more flexible and creative
- Landlords may be more flexible in extending time for assumption
- “Split Up” of business may be value maximizing
 - Online only
 - Owned real estate
 - Brand

Tomorrow:

- What might retail bankruptcies look like?
- Where sponsors have made use of unrestricted subsidiaries, we might see on effective abandonment of parts of business subject to liens (see PetSmart/Chewy Example)
- The use of bankruptcy remote IP holdco’s may also shift negotiating leverage

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Outline for Discussion

Increase in UST Section 1930 Statutory Fees

The Effects on Mid-size Bankruptcy Reorganizations – and status of current challenges to those fees

Intro – What is the purpose of the Bankruptcy Code (specifically Chapter 11 for business bankruptcies) – what do we have that is unique from other countries? The goal of rehabilitation of struggling corporate entities– and the recognition that creating a smaller more efficient company, or a better capitalized company, is better than liquidating a company which results in losing jobs, etc.

Regardless of whether it is possible to rehabilitate a company- the other primary goal is maximizing return to stakeholders. As an attorney representing a debtor we all owe a fiduciary duty to the estate – which includes creditors and equity. All professionals involved, whether they represent debtor, Committee, equity or other stakeholder, want to increase recovery.

The UST office, as part of this system, is supposed to support this mission – but has extreme increase on fees, and their aggressive enforcement and interpretation of fee statutes put them at odds with these essential goals? (Sidebar - Did the problem really begin with 1996 amendment that continued fees after confirmation – what does the UST do after confirmation? Why are they needed?)

A. History of the UST Program

1. Why and when was it created – 1990 test program
2. Funding - why self funding
3. UST v. BA
4. GAO report
5. Efficacy of program – are they a watchdog or just a transaction cost? IS the primary purpose to continue their existence or actually help people reorganize

B. The 2018 Fee Increase

1. Amount of increase
2. Effect on debtors – mid-range – exponential 800% increase in fees
3. Retroactive effect for Debtors already filed – antithetical to all we understand about due process
4. Exemption for the BA jurisdictions

C. Challenges to the Payment of Increased Fees

1. Definition of “Distribution” Crangrow – bankruptcy opinion and reversal by 7th Circuit (Danny’s market language) – how is that related to bk or the courts? Buffets also challenged definition (discuss issue of difference between liquidating trust and reorganized debtor)
2. Unconstitutional based upon Uniformity clause –
 - a. Buffets – opinion below – status of appeal (resolved by Sept?)
 - b. Circuit City – bk opinion found the fee increase unconstitutional based upon the Bankruptcy Clause as well as Uniformity Clause - This means the UST loses whether you call it a User fee or a Tax

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- c. Note that BAP reluctance to sign on to 1930 increase was based upon actual concern that these fees would kill mid-sized reorgs and force them to convert or dismiss – cites to Clinton Reply brief
- 3. Life Partners – Judge has kicked until 5t Circuit rules on Buffets
- 4. Acadiana vs. USA – Class action complaint based upon Uniformity Clause – Tucker Act
- 5. Unconstitutional because retroactive– Buffets and Acadiana
- 6. Clinton Nurseries -
- D. Practice Tips going forward
 - 1. Pre-packs – setting new records for how fast cases are in and out – Full Beauty
 - 2. Dismissing the bulk of open cases – Arch Coal
 - 3. Structuring around the statute – how to insulate distributions
 - 4. Entering a final decree but keeping AP's open? (Claire's) Note UST are objecting to Final Decrees – just so they can get fees.
 - 5. Don't structure bifurcated payment –make sure that the party making decisions about how fast to prosecute the case has to pay the fees. (Buffet's problem).
- E. Commentary – Why is UST so Aggressive? Using taxpayer dollars to appeal these cases. Should there be an appeal to Congress to fix it? What should we as the bar be doing?

Random thoughts – Should the US government be spending tax dollars to continually litigate whether these challenges should be brought via contested matter vs. Adversary proceeding (Clinton & Circuit City). Elevating form over substance is not a good use of public funds. All that should matter is the merits of the arguments. (paragraph 10 of Clinton reply brief)