

BANKRUPTCY OUTLINE

BASIC COMPONENTS OF A BANKRUPTCY

The basic components of a bankruptcy consist of the parties involved, which can have broadly different interests, the purposes of the bankruptcy, and the processes, which can be broken down into three distinct phases – the first days following the bankruptcy, the period needed to administer the estate, and the filing and confirmation of a plan of reorganization.

Though the parties, the purposes and the processes are generally the same, each case is unique and will vary based upon the size of the company, the number of Creditors, the amount of the debt and the financial condition of the company.

PARTIES

The parties can be defined as follows:

- a. Debtor -- Upon filing its bankruptcy petition the company formally becomes a Debtor; if no trustee has been appointed to take control of the bankrupt estate, the company is referred to as a Debtor in possession.
- b. Creditor -- Individuals, companies, and other entities to which the Debtor owes money and thus are considered to have a claim against the Debtor. There are two kinds of Creditors:
 1. *Secured Creditor* -- Those entities whose debt is protected by security or collateral.
 2. *Unsecured Creditor* -- Including among others lenders, suppliers, bondholders, and employees.
- c. Shareholders -- Owners of stock that was issued before the filing.

PURPOSES OF A BANKRUPTCY

For the Debtor the purpose of a bankruptcy is to allow it to reorganize its financial and operational structure so that it can emerge from bankruptcy court protection as a viable enterprise. For the Creditor the purpose would be to maximize the recovery on their claims.

The goals of the Debtor and the Creditor can either be in harmony or conflict with each other. Here are some examples:

Harmony -- Both the Debtor and the Creditor believe that a maximum recovery on claims can be achieved through reorganization, enabling the company to pay off the largest possible percentage of its debt through the generation of new revenue and equity.

Conflict -- The *Creditor* has concluded that they would receive a higher recovery if the estate were to liquidate while the *Debtor* continues to believe that reorganization holds out the best hope.

PHASES OF A BANKRUPTCY

FIRST PHASE

In the first days following the filing of the bankruptcy petition a distinct and critical dividing line is created between those events and actions occurring before the bankruptcy petition was filed (pre-petition) and the ones after the filing of the petition (post-petition).

Automatic Stay -- The Automatic Stay is triggered upon the filing of the bankruptcy petition. This action creates a shield around the Debtor and no one can commence or continue a judicial, an administrative or any other action against it.

First Day Motions -- In bankruptcy a Debtor is prohibited from making any payments to any creditor for any debt that accrued pre-petition, however, the Debtor must be able to pay amounts owed to the Creditor whose services or products are critical to the continued operation of the estate. As a result the Debtor files a number of motions asking the court to authorize it to make payments to these essential providers.

Within fifteen days of the filing unless extended by the court, the Debtor is required to file a list of Creditors, a schedule of assets and liabilities, current income, current expenditures and a Statement of Financial Affairs. The Debtor also seeks and hopefully secures Debtor-In-Possession (DIP) financing to enable the company to sustain its operations in bankruptcy. Entities providing DIP are willing to take a risk on a bankrupt company because the amounts owed to this lender are paid before any other creditor.

Selection of Creditor Committee by U.S. Trustee -- The U. S. Trustee, who is a government official, selects a Creditor Committee that consists of the seven largest Creditors, as well as other Creditors including in many cases, Labor Unions.

The Creditor Committee will retain its own attorneys, financial consultants and other professional advisors; these are paid for by the Debtor, and the function of the Committee is to ensure that the interests of all unsecured Creditors are fairly and fully represented.



SECOND PHASE

Administering the Estate. The Debtor must continue to operate its business and address all the claims and other matters that result from the bankruptcy filing.

Bar Date -- The Debtor must establish a deadline, referred to as a "Bar Date" by which time all Creditors must file their claims.

Executory Contracts -- The Debtor must determine whether to assume or reject contracts for which performance by the Debtor or the other party is required. Gate Gourmet for example. Services. Such contracts are referred to as "Executory Contracts". If the Debtor assumes an Executory Contract it must pay the outstanding amounts owed. If it rejects these liabilities, the amounts owed are treated as a claim against the Debtor. The bankruptcy court must approve assumption or rejection of an Executory Contract.

Aircraft Leases -- The Bankruptcy Code gives the Debtor sixty days after the filing of the bankruptcy petition to determine whether to assume or reject any of its aircraft leases.

Collective Bargaining Agreement (CBA) -- While CBAs remains in effect, arbitration provisions remain in force, and are unaffected by the Automatic Stay.

Section 1113 -- After filing a bankruptcy petition but before an application to reject a Collective Bargaining Agreement is filed, the Debtor must make a proposal to the Union that provides for modifications to the CBA that would be necessary to permit reorganization and treat all parties fairly and equitably. The Debtor must provide the Union with such relevant information as is necessary to evaluate the proposal. Please be aware that modifications to our Contract during a bankruptcy can be far more drastic and costly than the ones we had just ratified. Negotiations during a bankruptcy is considered more of a "Draconian Process"

Once the proposal has been made, and up until the rejection hearing, the Debtor must meet at reasonable times with the Union and confer in good faith in an attempt to reach mutually satisfactory modifications to the CBA.

Rejection of the CBA is permitted if the Debtor has satisfied the above criteria, the Union has refused to accept proposal without "good cause" and the balance of equities clearly favors rejection.

Once application to reject is filed, Bankruptcy Court must schedule a hearing within 14 days. (A seven-day extension can be granted without the consent of the both parties, or a longer extension can occur if both parties agree). The Bankruptcy Court must make a decision within 30 days from the date the court begins it's hearing on the Section 1113 application. It is very important to note that the Bankruptcy Court gives the company every advantage. The Court in not interested in justice, they're only interested in working with the Debtor to assure it comes out of bankruptcy as a profitable enterprise.

Section 1114 --This section only applies to retiree health benefits. The procedures to modify are very similar to Section 1113.

Sale of Assets -- Generally, the sale of substantial assets must be approved by the Bankruptcy Court with notice and hearing to all parties in the case.

THIRD PHASE

Bankruptcy concludes with the confirmation of a Plan of Reorganization, or if one cannot be confirmed the company may be liquidated or sold.

Plan of Reorganization -- The Debtor must prepare a Plan of Reorganization and a Disclosure Statement. The Plan of Reorganization (POR) primarily describes how the claims of each class of Creditors will be treated; it sets out the amount that will be paid, the schedule for paying the claim and the form of the payment. The Debtor can offer to resolve a claim by paying the creditor in cash, or it can provide new bonds or equity that it will issue after it emerges from bankruptcy. The Debtor will attempt to resolve as many claims as possible prior to actually filing the POR so as to increase the likelihood that the POR will be confirmed.

The Debtor is bound by very strict rules of the Bankruptcy Code in determining the treatment of Creditors. The Bankruptcy Code establishes the priority or the order of payment for each class of Creditor. A Creditor who holds a lower position in the order of payment cannot receive any recovery on his claim unless the Creditors who have a higher priority are paid in full.

In the POR, the Debtor must provide information sufficiently adequate to allow Creditors to make an informed judgment on whether to confirm or reject the POR. In the Disclosure Statement the Debtor submits what is fundamentally a business plan so that the Creditors and the court can assess whether or not the confirmation of the Plan would be followed by the liquidation of the Debtor or the need for another financial reorganization.

The POR must be approved by each class of Creditor, with 66% of the total amount of claims and 50% of total number of claims voting for confirmation.

Effect of Bankruptcy Confirmation -- Debtor's new financial life begins when the Bankruptcy Court confirms a POR and discharges the Debtor from debts that arose prior to confirmation as provided for in the POR.