

EFFECTS OF BAPCPA ON RETAIL CHAPTER 11s¹

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Can a retailer avoid a 363 or GOB sale post-BAPCPA? Many unrelated factors may force a retailer to file for bankruptcy protection, such as scarcity of capital following the credit crisis, overleveraged capital structure, decreased value of leasehold interests, competition from large discount retailers, and impacts from other tenants in a development, among others. However, BAPCPA's creditor friendly amendments also clearly impacted a retailer's ability to reorganize in Chapter 11. Although not impossible, the common thread to the handful of retailers successfully reorganizing in Chapter 11 since the enactment of BAPCPA is the lead time and planning before the filing – preplanning, preplanning, preplanning.

The goal is to strive for a prepackaged plan as close as you possibly can at the time of filing bankruptcy. Timing of the bankruptcy filing is also essential for retailers post-BAPCPA. All too often troubled retailers seek professional assistance and file for bankruptcy protection at the same time. The amendments in BAPCPA have significantly constrained a retailer's ability to reorganize absent substantial prepetition planning. In fact most retail cases have taken one of two paths: either the case is filed as a liquidation or the debtor is allowed a small window to conduct a going concern sale under 11 U.S.C. § 363, which typically only generates sufficient value to cover administrative claims and secured creditors.

The most significant changes in the Bankruptcy Code affecting retailers include: (1) shortened time under 11 U.S.C. § 365(d)(4) to assume or reject a real property lease to a maximum of 210 days; (2) increased cash demands for adequate assurance of future payments to utilities within 20 days of filing; (3) additional administrative claims for goods received by the debtor within 20 days of filing for the value of the goods (such claim must be satisfied to confirm the plan of reorganization); and (4) limited periods for the debtor to exclusively file and solicit plan acceptances. These amendments have decreased the time period a debtor has to get a handle on the company's financial position, and have impaired the retailer's ability to obtain necessary post-petition financing and breathing room from creditors to test and implement a reorganization strategy.

Chapter 11 retailers are more vulnerable following the enactment of BAPCPA, and as a result, most find post-petition financing nonexistent. Prior to BAPCPA a lender was assured that the retailer had sufficient time through routine extensions of the assumption/rejection period to analyze each lease before deciding to assume or reject. In addition, lenders were more likely to finance the debtor's reorganization due to the prior Bankruptcy Code provisions allowing an indefinite period of time to market and assign the below-market leases or to conduct a going-out-of-business (GOB) sale if the reorganization process was terminated, with sufficient time to implement sale procedures.

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BAPCPA severely restricted a retailer under the amended 11 U.S.C. § 365(d)(4), making it difficult for a debtor to have a full and fair opportunity to evaluate its commercial leases as necessary or burdensome. Now a debtor is required to assume or reject its real property leases within 120 days of filing, subject to one additional 90-day court approved extension. After that, extensions beyond the initial 210-day period may only be granted with the written consent of the landlord. Since retailers are no longer afforded an indefinite time line to judge the vitality of their business, lenders are extremely reluctant to give retailers financing, and they fear that there will not be enough time to conduct a GOB sale rather than a quick liquidation or go-dark scenario. Now, a retailer filing a Chapter 11 case without advanced planning must quickly decide to assume or reject its leases in roughly three to four months to allow enough time to conduct GOB sales if the need arises. Faced with this daunting task, a retail bankruptcy case's success may also hinge on the time of year the Chapter 11 protection is sought.

Which path a retail case takes often turns on the timing of the bankruptcy filing in relation to the proximity of the holiday shopping season. Retail filings in the second half of the year have little time to propose a going concern sale with the busiest sales period of the year around the corner. In recent years, creditors have insisted that retailers filing later in the year commence their GOB sales during the critical holiday season to maximize the value of the collateral. Alternatively, retailers that file bankruptcy earlier in the year may be provided the opportunity to develop a restructuring effort or adequately market the assets as a going concern without lenders' insistence on a quick liquidation to capture holiday sales.

Post-BAPCPA has shown that lenders are often simply unwilling to risk conducting a GOB sale after the holiday season. Existing lenders are also extremely reluctant to advance retailers a DIP loan, except for anything more than a nominal restructuring prior to conducting an orderly liquidation. What has proven to be true is that a retailer who adequately prepares before the filing is more likely to implement a plan and procedure, with the hope of drumming up as much support for its proposal as possible among its stakeholders, and benefiting from a relatively smooth bankruptcy process.

Retailers filing today without significant pre-filing planning lack the breathing room pre-BAPCPA debtors were afforded. To avoid a forced liquidation, adequate planning allows a retailer the benefit of implementing the solutions that are often negotiated before the filing, rather than finding solutions during a period of free fall. Proper planning affords a retailer the option of filing with a prepackaged or prenegotiated plan which could gain lender and trade vendor confidence, and avoid a forced fire-sale liquidation while working towards reorganization or a streamlined and well-organized going concern sale. Critical to prepetition planning is meeting with a professional to identify legal and business issues well in advance of the "crisis" stage.

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