Chapters 7, 11, and 13 Are Not Just in Books: Understanding Bankruptcy as a Surety Professional

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Bankruptcy Climate in 2020

• Energy
  • Chesapeake, Fieldwood, Arena Energy...

• Retail
  • Pier 1, Neiman Marcus, Tailored Brands...

• Hospitality/Entertainment
  • Pain Quotidien...
  • AMC Theatres?

• Transportation
  • Hertz, The Las Vegas Monorail Company...
  • Airlines?
Q1:2019 vs. Q1:2020
The Largest Cash Flow Declines Were in Two High-Leverage Industries

Source: American Bankruptcy Institute Newsroom (CRSP - COMPUSTAT Merged Database, Fundamentals Quarterly)
CHAPTER 7

• Liquidation
• Appointment of bankruptcy trustee to identify, collect, liquidate, and distribute assets
• Core tenets of “breathing space”; ratable distribution; and discharge apply

CHAPTER 13

• “Wage earner’s plan”
• Individuals or sole proprietorships
• Installment repayments over 3–5 years
• Appointment of trustee to whom Debtor makes plan payments
• Unsecured and secured debt thresholds for eligibility
CHAPTER 11

• Reorganization or liquidation
• Objective: Plan confirmation or reorganization
• Expensive
• Advent of the pre-pack

CHAPTER 15

• Modeled after UNCITRAL Model Law on Cross-Border Insolvency
• Recognition of foreign insolvency proceedings in U.S. Bankruptcy courts
• Key concepts:
  • Main vs. nonmain proceedings
  • Recognition
  • Post-recognition relief
SBRA: The New Small Business Bankruptcy

- New subchapter V of chapter 11 effective February 19, 2020 ("sub V case")
- Temporary increase of debt limits for eligibility under the CARES Act (from $2,725,625 to $7.5 million)
- Trustee, but with debtor in possession of assets and control of business
- Expedited administration:
  - 60-day status conference
  - Plan within 90 days; no disclosure statement
- Consensual plan -> Discharge (termination of the automatic stay)
- Cramdown plan -> Discharge to occur until completion of plan payments (3–5 years)

The Commercial Surety Account and Chapter 11
The Days and Months Before Bankruptcy...

What Can You Do?  Will It Work?

• Obtaining Collateral
  • Types of collateral
    • Letters of credit ("LOCs")
    • Cash
    • Security interest in receivables, etc.
  • Bankruptcy’s “preference” doctrine
• Types of collateral not created equal
  • LOCs and their proceeds:
    • Advantageous, but not invincible
Bankruptcy Is Filed

First Day Motions and Declarations

- Why?
- Utilities motion
- Debtor-in-possession ("DIP") financing motion
- Insurance and/or surety bond motion
Pendency of the Chapter 11 Case

- Debtor operations in Bankruptcy
- Surety exposure likely Increases
- Continued role of underwriting, account agent-broker
- Bond continuation or renewal
- Bond cancellation
- Post-petition surety credit facility

Disclosure Statement and Plan

- Plan release, exculpation, and injunction provisions

- Post-confirmation issues
  - New indemnity agreements/collateral agreements needed?
  - Return of collateral considerations
Collateral Swaps

#1: A distressed account requests that the surety’s existing LOC be cancelled, and the surety re-collateralized with an equivalent amount of cash.

ANY RISK?

#2: A distressed account requests that the surety accept an LOC in lieu of the cash presently held by the surety as collateral.

ANY RISK?
Underwriting Long Before the Threat of Bankruptcy

• The indemnity agreement
• Signed (and specific) financial statements
  • Non-dischargeability in bankruptcy
• The collateral agreement