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Private Equity Firms and Hedge Funds' Distressed Investing Strategies in Chapter 11 and Out-of-Court Corporate Restructuring and Distressed M&A

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A company files for Chapter 11 bankruptcy under the United States Bankruptcy Code in order to reorganize its business operations. While a company is in Chapter 11 bankruptcy protection, creditors may not pursue collections against the company for debt incurred prior to the bankruptcy filing, and thus, Chapter 11 provides the company with time to reorganize without constant threats from creditors.[1] Under Chapter 11, distressed companies can restructure the debt on their balance sheets and exit from bankruptcy stronger and with leaner liabilities.

Overall, for the year 2017, large companies filed for Chapter 11 bankruptcy protection less than the previous two years.[2] The total number of Chapter 11 filings has been approximately 7,000 cases for each of the last four years.[3] For the third year in a row, in 2017, companies in the oil and gas sector had the highest number of Chapter 11 filings.[4] Retailers had an unusually high number of Chapter 11 filings during 2017.[5] At least 30 major retailers filed for bankruptcy in 2017.[6]

Recently, private equity firms have been linked to several retail bankruptcies, including Payless Shoe Source, True Religion Apparel, and Toys "R" Us.[7] In 2005, the private equity firms Kohlberg Kravis Roberts & Co. L.P. (KKR), Bain Capital, and Vornado Realty Trust led a leveraged buyout (LBO) of Toys "R" Us. In an LBO transaction, most of the financing comes from a loan funded by the target company in order to buyout the existing public shareholders.[8]

As a result of the LBO, Toys "R" Us was highly leveraged and struggled to pay down the debt, which led to its filing for Chapter 11 on September 18, 2017.[9] In March of this year, after failing to reach a debt restructuring deal with creditors and unable to find a buyer or investor such as a private equity firm willing to provide new financing, Toys "R" Us was unable to reorganize in Chapter 11 and announced that it would sell or close all of its US stores.[10] However, according to reports, it is still possible that a new buyer or investor may emerge in time to rescue Toys "R" Us.[11]

In and out of Chapter 11, private equity firms and hedge funds frequently employ distressed

investing strategies. Distressed investing includes the buying or selling of equity or debt securities, bank debt, credit default swaps, or credit claims of companies under financial distress.[12] This article will discuss private equity firms' and hedge funds' distressed investing strategies in Chapter 11 court proceedings and out-of-court transactions, including strategies for acquiring control of distressed companies and other distressed investing strategies.[13]

Distressed M&A

For the purposes of distressed mergers and acquisitions (M&A), the term "distress" means a company that is experiencing difficulty handling its liabilities, such as making required payments on its loans, receiving or paying down trade credit, dealing with debt covenant breaches, or raising additional debt to deal with liquidity needs.[14] There are several different ways that a private equity firm or investor may acquire control of a target company, which is distressed, including buying assets, buying existing debt or providing new debt with the view that the debt will convert to equity of the newly reorganized company, merging with the target, or buying existing or newly issued stock.[15] Distressed M&A transactions can take many forms, including in-court and out-of-court M&A transactions.[16] Structuring a distressed transaction can depend on the target company's debt and capital structure, such as whether there is a single or multiple classes of secured debt, the urgency and degree of the target company's financing needs, how long the target company can preserve its relations with key employees, suppliers, and customers, consent rights of contractual parties such as lenders, lessors, and customers, and timing of loan or bond defaults.[17]

Although out-of-court M&A transactions often are quicker and less costly than in-court transactions, out-of-court transactions frequently require approval from shareholders or creditors and parties who do not consent to such transactions, and thus, are usually not bound to changes in their fundamental rights.[18] In contrast, an in-court M&A transaction can bind parties without their consent and does not require approval from shareholders. Thus, in-court transactions frequently are used for companies in financial distress.[19] Hybrid strategies—such as "prepackaged" and "pre-negotiated" reorganization plans—can be used for a distressed company with sufficient time to undergo out-of-court negotiations before entering court by filing for Chapter 11 reorganization.[20] Hybrid strategies often are quicker and less costly and result in less friction between parties and less risk of harm to the company, such as the risk of losing suppliers, employees and the risk of harm to the company's reputation with customers.[21] The threat posed by a distressed company's willingness to file for bankruptcy can be sufficient to induce dissenting creditors into agreeing to an out-of-court transaction.[22] Asset sales during bankruptcy, referred to as 363 sales, may be executed under §363 of the US Bankruptcy Code in an expedited manner.[23]

Control-Oriented Strategies

A private equity firm or investor has several methods for obtaining control of the distressed company, including:

1. "loan-to-own" transactions,
2. purchasing the main assets of the company via an asset purchase agreement, and
3. filing a competing plan of reorganization.[24]

In the private equity firm KKR's Form 10-K, it states that KKR seeks to "make opportunistic investments largely in distressed companies" through its "special situations investment strategy."[25] This strategy includes "distressed investments (including post-restructuring equity), control-oriented opportunities, rescue financing (debt or equity investments made to address covenant, maturity or liquidity issues), debtor-in-possession or exit financing, and other event-driven investments in debt or equity."[26] KKR reports that it had assets under management of $7.4 billion in this strategy as of December 31, 2017.[27]

A company that enters into Chapter 11 for corporate reorganization is referred to as the

"debtor-in-possession." Many companies go bankrupt because of a lack of immediate liquidity.[28] Debtor-in-possession (DIP) financing is new debt that a target company obtains while reorganizing under Chapter 11.[29] The DIP financing has priority over existing debt, equity, and other credit claims.[30]

"Loan-to-Own" Transactions

Frequently, private equity firms and other investors engage in loan-to-own transactions. Loan-to-own transactions have many forms, including buying existing debt claims from creditors of the company or providing DIP financing to the distressed company with the view of the debt converting to a controlling equity position in the company after it reorganizes and emerges from bankruptcy under Chapter 11.[31] By buying a strategic position in existing debt or providing DIP financing, the investor may obtain leverage in reorganization plan negotiations and help the investor with gaining control of the company.[32]

An investor engaging in a loan-to-own strategy via acquiring existing debt must first determine which debt security or instrument is the "fulcrum security."[33] The fulcrum security is the security that will convert into equity once the distressed company has reorganized. In order to determine which security or instrument is likely the fulcrum security, an investor must determine the value of the distressed company and identify the debt security or instrument that will receive the new equity issued by the reorganized company. Determining the fulcrum security is more of an art than a science.

Depending on the capital structure of the company and company's valuation, the fulcrum security could be first or second lien debt, senior unsecured bonds, subordinated bonds, or trade claims.[34] Private equity firms and hedge funds often carry out a loan-to-own strategy by buying second lien secured debt.[35] However, debt acquisition strategies for control depend on the unique capital structure and valuation of a distressed company.[36] Thus, depending on the financial circumstances of a distressed company, a private equity firm or hedge fund may buy different classes of debt of the target company.

An investor who purchases debt that is too senior is at risk of receiving only cash or assets from the distressed company without receiving an equity stake. An investor who purchases debt that is too junior is at risk of receiving less or no equity in the target company once it reorganizes. To mitigate these risks, investors often purchase different classes of debt of the target company. Determining the likely fulcrum security is complex and several factors influence which class of debt security or instrument will eventually be the fulcrum security. Some of these factors include (1) the target company's cash flow and liquidity, (2) the rights of debt holders under the debt agreements (for example, to call default or accelerate debt), (3) the relative rights of senior and junior creditors under intercreditor agreements, and (4) whether the debt holders are willing to participant in a reorganization.[37]

Sometimes, a bank lender reluctantly ends up holding the fulcrum security.[38] For example, Bank of America and other first lien lenders ended up receiving all of the new equity of the bankrupt company UTGR Inc. that operates the Twin River Casino in Lincoln, RI.[39] When the bankrupt company was unable to find a buyer, Bank of America and other first lien lenders become the sole equity holders when the federal bankruptcy court approved UTGR Inc.'s bankruptcy plan to give all its new equity, which is issued by UTGR Inc. after it reorganizes, to the lenders in exchange for forgiving $442.4 million in debt and a new senior secured first lien credit facility of $300 million.[40]

While the target company is moving through its reorganization process and negotiations, its earnings before interest, taxes, depreciation, and amortization (EBITDA) and underlying circumstances may change, and thus the valuation of the company may change. As a result, the fulcrum security may change during the reorganization process.[41] Also if the private equity firm or other investor's valuation analysis

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is not accurate, a different debt class of creditors may hold the fulcrum security.[42]

An investor that buys a sufficient amount of the fulcrum security can attain a "blocking position," and as a result, the investor may be in a position to negotiate the reorganization plan with the company and creditors committee.[43] To approve a reorganization plan, there must be approval of at least two-thirds of the dollar amount of the debt claims and the majority in number of debt claims for each accepting class.[44] Thus, an investor that purchases one-third in amount of the debt claims has significant influence on reorganization plan negotiations because the investor is in position to block the acceptance of the plan.[45] Frequently, a blocking position may be obtained by an investor with less than one-third of the total amount of debt claims because only debt claims that are actually voted count.[46] However, if an investor obtains a blocking or control position and uses that position in a manner that is solely for its benefit without a benefit to the class to which it belongs, the investor runs the risk that the investor's votes may be disqualified and considered to be cast in bad faith.[47]

Loan-to-Own via DIP Financing

DIP financing is new financing that the distressed company can obtain while in Chapter 11 bankruptcy, provided that the bankruptcy court approves such financing.[48] Most companies in Chapter 11 require DIP financing in order for the company to continue operating during the Chapter 11 case and maintain the value of the enterprise.[49] Often, the distressed company will require new money via DIP financing to address its liquidity needs.[50] Existing debt instruments may place restrictions on how new financing is provided.

The US Bankruptcy Code allows a distressed company to place liens on its property that are senior to existing liens, provided that the existing lenders are adequately protected.[51] Also, if there is any deficiency in the value of collateral that secures the DIP financing, the DIP lender is given a claim that is of greater priority status for recovery in bankruptcy than pre-Chapter 11 and post-Chapter 11 unsecured debt.[52] As a result, the risk of loss for a DIP lender is low, and it is rare for a DIP lender to not be repaid in full.[53] Frequently, in a Chapter 11 reorganization case, an investor will have an opportunity to finance the Chapter 11 plan via DIP financing, which can allow the investor to gain control of the distressed company.[54]

Potential Debt-to-Equity Conversion Methods

A private equity firm or other investor engaging in a loan-to-own strategy, and thus acting as a creditor, should consider the potential best method of converting the acquired debt into equity including: (1) out-of-court exchange offers, (2) prepackaged Chapter 11 bankruptcy plans, (3) pre-negotiated Chapter 11 plans, and (4) post-bankruptcy debt acquisitions.[55]

The first option, an out-of-court exchange offer, allows consenting creditors, such as private equity firms or hedge funds who purchased debt or provided DIP financing to the company, to exchange their debt for equity.[56] An exchange offer can be registered or unregistered.[57] In the case of a public company, exchange offers can be further complicated if the company is required to generally solicit votes of shareholders via a proxy statement.[58] Second, in a prepackaged Chapter 11 bankruptcy plan, impaired classes of creditors, which may include a private equity firm or hedge fund, agree prior to a filing for bankruptcy to convert their debt to equity in accordance with a plan of reorganization that is solicited and approved by creditors prior to filing for bankruptcy.[59] A prepackaged bankruptcy may be quicker and less expensive than a traditional bankruptcy.[60] However, as explained later, prepackaged bankruptcies have potential complications; a pre-negotiated plan may be a better option.

Third, in a pre-negotiated Chapter 11 bankruptcy plan, impaired classes of creditors, which may include a private equity firm or other investor, agree to the basic terms of a reorganization plan

prior to the filing for reorganization under Chapter 11 by signing a plan support agreement, as discussed below.[61] Fourth, in a post-bankruptcy debt acquisition, existing creditors and other investors buy debt claims after a filing for bankruptcy for the purpose of gaining some influence over the reorganization plan process, such as voting rights with the intent of converting the purchased debt into newly issued equity in the company after it reorganizes.[62]

Asset Sale Deal Structuring Options

An investor may opt to structure the acquisition as a purchase of a distressed company's assets rather than buying debt or equity. An out-of-court asset sale is a sale via an asset purchase agreement that can be a good option provided that the target company has a simple debt structure, consent is not needed from third parties and the government or such consent can readily be obtained, and the target company's fiduciaries see low risk of liability posed to them by approving such a sale.[63] Under such circumstances, an out-of-court sale can allow the parties to keep transaction costs to a minimum and quickly close the transaction.[64]

Another option is an in-court "363 sale" of assets pursuant to §363 of the US Bankruptcy Code. For a 363 sale of assets, in the first step, the company obtains the bankruptcy court's approval of the auction procedures, such as the bid protections for a "stalking horse" bidder.[65] A "stalking horse" is an initial bidder, which may be a private equity firm or other creditor, that makes an offer for the target company's assets and the target company uses such offer to solicit competing offers, typically in an auction process.[66] The stalking horse bidder and distressed company negotiate an asset purchase agreement that includes the terms and conditions of the initial bid.[67] In the next step of a 363 sale, the distressed company holds an auction for bidders, including the stalking horse bidder.[68] During the first and second steps, the company and proposed buyer should negotiate an asset purchase agreement, conduct due diligence, and, if necessary, obtain financing and regulatory approval.[69]

In a 363 sale of assets, the bankruptcy court will approve the highest and most qualified bidder as the purchaser.[70] If the stalking horse bidder loses to a competing bidder, the stalking horse bidder will receive its breakup fee and expense reimbursement.[71] In addition to being typically completed quickly, a primary advantage of a 363 sale of assets is that the sale will be free of liens, claims, and interests and well protected from challenges because it has the approval of a bankruptcy court.[72]

An investor that acquires control of the company by providing DIP financing of a reorganization plan may have more flexibility than via a 363 sale of assets. In contrast to a 363 sale of assets, a Chapter 11 plan permits liabilities to be satisfied in exchange for newly issued equity and new debt agreements.[73] Unlike a Chapter 11 plan financing, in a 363 sale of assets, generally, the buyer can purchase the assets only with cash.[74] However, generally, the disadvantages of the Chapter 11 plan process are that it takes substantially more time and that it is more complicated and expensive than a 363 sale of assets.[75]

Proposing a Competing Plan

In certain situations, a creditor may propose a competing reorganization plan in opposition to the company's proposed plan.[76] An investor should keep in mind that the Chapter 11 process is heavily in favor of the distressed company when considering to propose a non-consensual plan.[77]

The distressed company has several advantages, including access to information, having the incumbent management and board, and an exclusive period of up to 18 months after the bankruptcy filing date. During the exclusive period, only the distressed company is allowed to propose a plan of reorganization; with the exception of the case where the exclusive period is terminated for cause, which in practice is difficult to obtain.[78] After the exclusive period ends, an investor may propose a competing plan of organization, which can give the

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investor significant leverage in the negotiations of a consensual plan.[79]

By formulating the Chapter 11 plan of reorganization of a distressed company to execute a loan-to-own strategy via debt acquisition or DIP financing, a private equity firm works with the management team of the company to decide on a plan for the newly reorganized company's balance sheet, including post-restructuring debt and equity.[80] A plan of reorganization is subject to court approval and is required to designate classes of claims; generally, the classes will be: (1) secured creditors, (2) unsecured creditors, and (3) equity security holders.[81] The US Bankruptcy Code requires that, for the court to confirm a plan, the reorganization plan must (1) be accepted by at least one class of non-insiders who hold impaired claims, which are claims that will not be paid entirely or for which some legal, equitable, or contractual right is altered, (2) not unfairly discriminate, and (3) be equitable and fair.[82]

Generally, only claims that are "impaired" under §1124 of the US Bankruptcy Code may vote on the confirmation of the plan.[83] A claim is deemed to be unimpaired if the plan "leaves unaltered the legal, equitable, and contractual rights to which such claim or interest entitles the holder of such claim or interest."[84] The bankruptcy court can confirm a plan consensually by approval of all the impaired claim holders. A plan that a court confirms non-consensually is called a "cramdown."[85] Cramdown allows for the court to confirm a reorganization plan despite one or more classes of creditors or equity holders rejecting the plan.[86]

Valuation Disputes

Disputes over valuation arise frequently in distressed investing. Valuations are subject to differing methodologies and party interests.[87] Valuation is often the most disputed element in corporate bankruptcy.[88] Particularly when the stakes are high, valuation can be manipulated to serve the interests of a party in bankruptcy, such as a private equity firm or hedge fund.[89] Since the class of debt that ends up being the fulcrum security depends on the valuation of the distressed company, a private equity firm or hedge fund engaging in a loan-to-own strategy has self interest in a valuation fight.[90]

The basic methods of valuation of a distressed company are based on: (1) what buyers have paid for a similar company previously, (2) discounted future cash flows, (3) company earnings, (4) market price of the target company's equity and debt securities, and (5) a combination of these methods, a hybrid approach.[91]

Valuation of the distressed company's enterprise value depends on several factors, including the uncertainty of future circumstances.[92] Faced with such uncertainty, the value of the company in the plan becomes a subject of negotiation.[93] A bankruptcy court assesses whether the valuations in a proposed plan are reasonable, and as a result, many reorganization plans within a range of values for the distressed company are confirmable.[94]

Intercreditor Agreements

Private equity firms and hedge funds have played a major role in the development of the second lien loan market.[95] A second lien loan is a loan that is secured by collateral, but is less senior than a first lien loan in priority of recovery. Second lien loans are secured debt and are next in priority after a first lien loan, but with greater priority of recovery than unsecured creditors. Typically, the first lien lender seeks to recover the principal and interest of the loan. Often, the first lien lender will receive the total residual value of the distressed company, and thus making the second lien loans the fulcrum security to receive the new equity of the reorganized company emerging from bankruptcy.[96] Frequently, private equity firms and hedge funds as lenders provide second lien loans with detailed intercreditor agreements that try to control and direct the rights and remedies of the holders of first and second lien loans.[97] For instance, an intercreditor agreement could include detailed provisions concerning insolvency, refinancing, a liquidity event, and default.[98]

Intercreditor agreements are frequently used to define the relationships between secured creditors at differing levels of seniority such as the first and second lien loan holders.[99] An intercreditor agreement defines the rights of each creditor with respect to the priority of payment or liens and could be multiple agreements or a single agreement.[100] Thus, it is imperative for a private equity firm or other investor to review the intercreditor agreement if they are seeking to invest in debt of a distressed company that has multiple levels of secured debt.[101]

Typically, a first lien lender's foremost priority in an intercreditor agreement is to ensure that it will obtain payment from the collateral of principal and interest before the second lien lenders.[102] In order to accomplish this, first lien lenders often try to stop the second lien lenders from being able to enforce their remedies until the first lien debt is completely satisfied.[103] Also, first lien lenders frequently try to limit second lien lenders' ability to take action that would obstruct the first lien lenders control of the collateral after a default or during bankruptcy.[104]

Intercreditor agreements are considered to be subordination agreements.[105] Under §510(a) of the US Bankruptcy Code, a subordination agreement is enforceable just as it would be enforced under non-bankruptcy law.[106] Thus, bankruptcy courts generally enforce intercreditor agreements.[107]

PIPE Investment Offerings

Another option for raising capital that a distressed company may seek is a private investment in public equity (PIPE) investment offering.[108] A PIPE investment offering is a private placement of securities of an already public company that usually is made to institutional accredited investors, such as a private equity firm or hedge fund.[109] In a PIPE investment, usually an investor buys new securities from the distressed company at a discount to the current market price.[110] The new securities could be common stock, preferred stock, unsecured notes, which are convertible to common stock, or other securities.[111] The private equity firm or other investor may receive governance rights that include a right to designate one or more directors on the distressed company's board of directors.[112]

Credit Default Swaps

Private equity firms that employ distressed investing strategies may purchase credit default swaps to hedge against the risk of debt default if they own the underlying debt or to speculate if they do not own the underlying debt. In the Form ADV for KKR Credit Advisors (U.S.) LLC, it states that KKR's credit funds "may invest in credit default swaps for hedging and investment purposes."[113] A credit default swap is an agreement between two parties that transfers the risk of loss if a debt issuer, such as a distressed company, fails to timely pay principal or interest under a debt agreement or files for bankruptcy.[114]

Stated another way, a credit default swap is a contract between two parties, a buyer and a seller, typically a bank or insurance company; the seller is providing a financial product, which functions like insurance, to the purchasing party who will be paid in the event that a debt issuer, or a financial instrument, fails.[115] In KKR's Form ADV, it states that KKR's credit funds may buy credit default swaps even when KKR's credit funds do not own the underlying debt security or instrument if there is high likelihood of credit default.[116]

Competing Agendas & Objectives in Distressed Situations

A distressed company and its advisors are often subject to many parties, including private equity firms, hedge funds, bondholders, secured lenders, trade creditors, and shareholders, with competing agendas and objectives.[117] Investors buy distressed debt for many reasons, including when such debt is perceived to be under-valued or as part of a strategy to takeover a distressed company.[118] Distressed debt is debt obligations that are in default or are perceived as near default.[119] Distressed debt can be

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secured or unsecured debt and can be any debt, such as trade claims, contract claims, or funded debt.[120] Private equity firms or other investors may buy distressed debt to apply leverage over distressed companies and lenders.[121] For instance, if a private equity firm buys a substantial amount of secured debt of a target company, the private equity firm may be able to influence the target company to file for Chapter 11 and influence the decisions of the secured lenders.[122]

Lenders frequently demand substantial information about a company and its restructuring by means of the rights provided in the original loan documents or in an agreement to forbear on their rights after a company is in default on its loan obligations.[123] For instance, bondholders often include two different groups: par holders, which purchased the originally issued bonds, and "vulture investors," which are typically private equity firms and hedge funds.[124] Bondholder groups can use numerous means to exert pressure on a distressed company, including:

1. Threatening litigation if the debtor company does not adhere to their demand and/or fails to run the company or restructuring to the advantage of the bondholders,
2. Seeking to limit any new financing that could harm the future recoveries of bondholders,
3. Demanding that the bondholders' favored crisis manager be hired to run the company,
4. Threatening to file an involuntary reorganization under Chapter 11, and
5. Soliciting outside M&A interest in the debtor company.[125]

As required under the terms provided in credit agreements, secured lenders have access to new and continuing material non-public financial information from the borrowing company.[126] Thus, secured lenders typically know of impending financial and operational issues before bondholders, trade creditors, and shareholders.[127]

The existing shareholders, also referred to as "old equity," are usually more passive than the other constituency groups. However, for private companies with shareholders that have controlling equity positions, such shareholders may have influence on the board of directors.[128]

Prepackaged & Pre-Negotiated Plans of Reorganization

In a prepackaged plan of reorganization, the solicitation and voting occur before the petition for bankruptcy is filed.[129] A prepackaged bankruptcy plan that involves the offering of new securities raises an unsettled issue as to whether the new securities offering would be exempt from the registration requirements of the Securities Act of 1933.[130] Section 1145(a) of the US Bankruptcy Code provides an exemption from registration for a securities offering. Under the Securities Act, a new securities offering must either be registered or have an exemption from registration.[131] There is uncertainty as to whether the §1145 exemption applies to a solicitation of votes that is conducted before petitioning for bankruptcy because the text of §1145 exempts only "a security of the debtor" from registration, and under the US Bankruptcy Code, an issuer is not a "debtor" until a Chapter 11 case commences.[132]

Unlike a prepackaged plan of reorganization, in a pre-negotiated reorganization plan the solicitation and voting take place after the petition for bankruptcy is filed, and thus the pre-negotiated plan is not subject to the uncertainty as to the application of §1145.[133] The SEC Staff informally has stated previously that the §1145 exemption is unavailable for prepackaged bankruptcy plans.[134] In addition to securities law considerations, prepackaged bankruptcy plans may violate certain requirements of the US Bankruptcy Code concerning bankruptcy plans, such as the requirement of soliciting beneficial holders of securities and also that record holders need to demonstrate that they have authority to vote securities that are in their names.[135] Given that a prepackaged plan's disclosure and solicitation

process, which takes place pre-bankruptcy, raises issues of legal uncertainty and has the potential to be rejected by a court, in recent years, distressed practitioners have moved toward the use of pre-negotiated plans.[136]

Plan Support Agreement

A pre-negotiated plan of reorganization is typically conducted with a plan support agreement. A plan support agreement, also called a lock-up agreement or restructuring support agreement, is an agreement between creditors or between creditors and a debtor company that controls how the creditors' claims will be voted or otherwise supported for a particular reorganization plan in Chapter 11 or in a 363 sale of assets.[137]

Also, a plan support agreement may restrict creditors from taking other actions, such as the filing of objections in Chapter 11.[138] Further, such agreements restrict a creditor's ability to trade its debt claims.[139] Such a restriction usually requires any buyer of a debt claim to agree to be bound to the terms of the plan support agreement.[140] Thus, a potential buyer of a debt claim, as part of its due diligence, should determine whether the seller is a party to a plan support agreement, and if so, the buyer should review the terms of the agreement with care.[141]

Equity holders, particularly in a closely or privately held company, can be required by parties to the negotiation to be a party in the plan support agreement.[142] Equity holders will likely recover nothing if the company is insolvent. However, equity holders likely have control of the distressed company via the board of directors.[143] In the closely or privately held company, the equity holders have the power to vote for and put a new board of directors in place that reflects the views of the equity holders.[144] Thus, in the closely or privately held company, the group of creditors to a plan support agreement will likely consider including equity holders as a party to the agreement in an attempt to avoid issues with the board and preempt the equity holders from taking opposing positions.[145]

In general, directors of the board have a fiduciary duty to ensure that the maximum value of the distressed company is recovered for the stakeholders.[146] By agreeing to the terms of the plan support agreement, the board is required to determine that the terms provided in the agreement will allow the board to fulfill its fiduciary duty.[147] Nevertheless, circumstances may change substantially.[148] For instance, the value of the distressed company changes over time, and thus the fulcrum security may shift to a different debt security or instrument.[149] In such case, the board may be required to take action that is not consistent with the terms of the plan support agreement.[150] As a matter of law, the agreement must allow the board to fulfill its fiduciary duty.[151] Typically, the agreement will provide a "fiduciary out."[152] However, the terms to which the board may exercise its fiduciary duty vary in plan support agreements.[153] In some cases, the plan support agreement provides that, if the board determines that it must terminate such an agreement for the board to exercise its fiduciary duty, then the board may do so.[154]

Acquisition Risks

In order to manage risk, a private equity firm, hedge fund, or other investor should, if feasible,

1. undergo thorough research to evaluate whether a debt claim is subject to any legal issues or actions by creditors or other stakeholders;
2. negotiate to obtain appropriate representations, warranties, covenants, and indemnities from the seller in the transaction and assignment documents;
3. negotiate for a purchase price holdback;[155]
4. buy an option instead of buying the debt claim; and
5. deal with sellers who are creditworthy.[156]

Commonly used distressed debt sale documentation includes representations, warranties,

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covenants, and indemnities; however, additional or amended representations, warranties, covenants, and indemnities may be appropriate depending on the facts and circumstances.[157]

Private equity firms, hedge funds, and other investors face potential acquisition risks via lawsuits based on claims of fraudulent conveyance, lender liability, equitable subordination, and/or recharacterization. In distressed company situations, creditors frequently pursue litigation strategies to increase their recoveries.[158] One of the most commonly used litigation strategies that creditors use is fraudulent conveyance.[159] A fraudulent conveyance occurs when a debtor company transfers value or incurs an obligation that is actually or constructively fraudulent by having the effect of transferring value from the debtor company that otherwise would be available for the company's creditors.[160] In bankruptcy, the US Bankruptcy Code or applicable state law will apply; in contrast, outside of bankruptcy, only state law will apply with respect to fraudulent conveyance.[161]

A private equity firm or investor acquiring debt or assets is subject to the risk that a court may find that the purchase price was less than "reasonably equivalent value" and invalidate the sale on the grounds of a fraudulent conveyance.[162] For instance, in the case *in re Bridgeport Holdings Inc.*, the Delaware bankruptcy court referred to the distressed company's sale as a "fire sale" of a significant portion of assets with the sale occurring only one day prior to the bankruptcy filing.[163] The Trustee brought a suit against the buyer on a claim of fraudulent conveyance, and the buyer ended up settling for $25 million, a substantial amount especially since the initial purchase price was $28 million.[164] Prior to the sale of assets, the buyer had valued the assets to be worth $126 million; over four times the purchase price.[165] Further, in the *Bridgeport* case, the court also held that the directors of the board, officers of Bridgeport, and an outside advisor had breached their fiduciary duties of loyalty and care in the asset sale.[166] The court held that the directors breached their duty of care by failing to obtain a valuation of the assets that were sold and by failing to sufficiently market the assets.[167]

There are many strategies to help mitigate the risk of litigation from a sale or spin-off of distressed assets.[168] For instance, the transacting parties should make efforts to ensure a record of a sale process that is conducted in a reasonable manner and in good faith at arm's length terms.[169] It may be helpful as part of the sale process for the company and the acquirer to obtain a capital adequacy, solvency, and/or valuation opinion from an expert third party. Such an opinion may be helpful in defending the sale against claims of fraudulent conveyance.[170] Further, a solvency opinion may be useful in demonstrating that a director approved a transaction in good faith fulfilling the director's fiduciary duties under Delaware state law.[171]

Lender liability is damages that are recoverable from a creditor where a court found the creditor to have acted unreasonably with exercising its remedies and may arise if a creditor's bad faith or negligence results in damage to a company.[172] For instance, a situation where lender liability occurs may include a creditor putting new management in place that mismanages the company or colludes with the creditor.[173] Creditors to a distressed company including a private equity firm or other investor may try to impose restrictions or coerce the company to take certain actions.[174] Such coerced actions may result in lender liability for the creditor, including liability for fraud, breach of fiduciary duty, breach of contract, or breach of implied covenant of good faith and fair dealing.[175]

The US Bankruptcy Code allows a bankruptcy court to "equitably subordinate" all or part of a creditor's claim, resulting in a lower priority status for recovery, in relation to the claims of other creditors to remedy harm due to inequitable conduct.[176] A private equity firm, affiliate, or insider of the target company which purchases debt of the target company can be subject to a creditor's lawsuit claiming that such debt should be "equitably subordinated"

if the company files for bankruptcy for reasons that the purchasing party controlled the target company and is culpable for the company's insolvency or some other misconduct.[177] In addition to the risk of equitable subordination, a private equity firm, affiliate, or insider of the target company, who purchases debt of the target company can also be subject to the risk that a bankruptcy court may recharacterize the purchased debt as equity; resulting in a lower priority status for recovery in bankruptcy.[178]

The securities laws apply to trading debt claims that are based on securities.[179] Some debt claims are not based on securities including, generally, trade debt and bank debt.[180] However, the definition of "security" under federal law as provided in the Securities Act of 1933 is perhaps sufficiently broad to include bank debt because it includes "any note" or "evidence of indebtedness."[181] Thus, investors and claims traders should consider the risks of trading any debt claims while holding material non-public information about a company.[182] Also, investors that buy debt claims may be subject to lawsuits based on private state law fraud claims.[183]

Members of an official committee of unsecured creditors owe fiduciary duties to each other and the constituencies that they represent.[184] For instance, if a private equity firm becomes a member of a committee of unsecured creditors and the private equity firm obtains material non-public information and based on such information buys or sells securities or other financial instruments, it may violate its fiduciary duties or securities laws.[185]

Generally, securities, which a reorganized company issues or sells pursuant to a Chapter 11 plan in exchange for debt claims against or interest in the company, are exempt from the registration requirements of the securities laws.[186] However, an investor that owns a substantial equity portion in the reorganized company or has significant influence over the company that results in the investor possibly being considered an "affiliate" of the company may not be permitted to make use of the exemption from registration.[187]

Big Boy Letter

For a purchase of debt or other securities where the seller or buyer has nonpublic information the parties should consider entering into a big boy letter agreement to mitigate the chance of, and protect against, a lawsuit.[188] A big boy letter is a letter agreement where the counterparty acknowledges that (1) it is a sophisticated actor in the market, (2) the insider may hold material non-public information, (3) the counterparty will not sue the insider concerning the insider's alleged use of material non-public information in the sale transaction, and (4) the counterparty is relying solely on its own research and analysis in entering in the purchase transaction.[189] However, there is a lack of case law addressing whether a big boy letter will be effective in protecting against liability.[190] Generally, law opposes any waiver of fraud claims in advance.

A big boy letter can help protect insider purchasers and sellers from liability to counterparties for claims based on common law fraud.[191] A claim of common law fraud generally has the elements of: (1) misrepresentation or concealment of a fact that is material, (2) scienter, (3) for which the other party justifiably relies on, and (4) results in injury.[192] In a big boy letter, the counterparty acknowledges that it is a sophisticated party not relying on the insider for information. This acknowledgement makes it more difficult for a party to prove that reliance was justifiable.[193] The elements of a private securities fraud claim are generally the same as a common law fraud claim including scienter and reliance. As with a common law fraud claim, in a private securities fraud claim, because the counterparty acknowledges that it is not relying on the insider for information the counterparty may have difficulty proving reliance was justifiable.[194]

If the buyer or seller is a fiduciary, this raises additional concerns, such as the debt claim being subject to equitable subordination and/or reduction or disallowance.[195] Usually, fiduciaries have access

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to non-public information, and as such their debt claims have an increased likelihood than unaffiliated creditors to be examined, objected to or lead to litigation.[196] An investor that receives inside information from an insider likely will cause the investor to become "restricted" and potentially considered to be an "insider," which will result in the investor being unable to trade or having trading restrictions. [197] In such case, a trade of a debt claim made with a big boy letter agreement may mitigate the chance of, and protect against, litigation.[198]

Insiders have a much greater chance of being the target of investigation for potential civil and criminal liability. Thus, the investor should undertake diligence on a seller who is an insider.[199] The investor's acquisition may be subject to equitable subordination and/or reduction or disallowance if the seller's debt claim would have been subject to it.[200] Thus, a private equity firm or investor, who intends to buy claims or interests of a distressed company in a Chapter 11 reorganization may be in a better position by not serving on a committee.[201] Nevertheless, committees frequently play a crucial role in shaping the reorganization of a Chapter 11 distressed company, and thus, an investor should consider this as well.[202] In such case, by using a big boy letter agreement, an investor that buys from a fiduciary may mitigate the possibility of, and protect against, litigation.[203]

Tax Attributes

When the distressed company's debt is canceled, forgiven, or discharged, the tax code generally provides that the company is required to include the amount of the canceled debt in its gross income, commonly referred to as cancellation of debt (COD) income subject to some exceptions.[204] There is an insolvency exception that provides that the COD income will not count as taxable income to the extent that the distressed company is insolvent immediately before the cancellation of debt.[205] For instance, under the insolvency exception, a company with liabilities of $100 and assets of $90 before $20 of the company's debt is canceled by its lender via an out-of-court restructuring will result in a recognized income of only $10 of taxable COD income despite $20 of debt that was canceled.[206] Likewise, the tax code exempts any COD income occurring in a reorganization case under Chapter 11.[207]

Often, a company restructures its debt so that new consideration provided by the company is worth substantially less than the face amount of the original debt.[208] As a result, the tax gain is equal to the value differential and can be offset by certain tax assets including net operating losses (NOLs) in both in-court and out-of-court restructurings.[209] NOLs represent prior losses that may be used to offset against taxable income in the future, and thus may be used to decrease a company's taxable income after it comes out of bankruptcy.[210]

While NOLs can be of great significance to minimize taxes for the restructured company, the company's ability to make use of NOLs is subject to rules concerning certain changes in equity ownership of the company under the Internal Revenue Code.[211] Bankruptcy courts have often ruled in favor of restricting the transfer of debt and equity because such transfer may put the company at risk of losing its NOLs.[212] A private equity firm or investor with a view to acquire a controlling position should assess the facts and circumstances of the purchase as it concerns NOLs.[213]

Conclusion

Private equity firms, hedge funds, and other investors have several different deal structuring options to choose from in carrying out a distressed investing strategy. These options include whether to purchase debt, assets, or equity in the target company and whether to undergo an out-of-court or in-court acquisition strategy via loan-to-own strategies or purchasing assets or stock.

Given the complexity and factors involved in each distressed investing situation, careful analysis of the surrounding facts and circumstances, including

the existing creditor agreements, relevant federal and state statutory and case law, valuation and tax issues, and other relevant legal and economic issues, as well as the stakeholder dynamics, is crucial to arrive at a well-conceived acquisition strategy.

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NOTES

1 11 U.S.C. §362(a). After the Chapter 11 bankruptcy petition is filed an automatic stay of creditor actions against the debtor company goes into effect. The automatic stay is a period of time that suspends all judgments and collection activities during which creditors may not pursue any debt or claim incurred before the Chapter 11 filing.

2 Samuel L. Gerdano and Ed Flynn, ABI 2017 Chapter 11 Review: Large Company Filings Down, Retail & Oil Still Show Distress, January/February 2018; available at: *http://www.abfjournal.com/articles/abi-2017-chapter-11-review-large-company-filings-down-retail-oil-still-show-distress/*.

3 *Id*.

4 *Id*.

5 *Id*.

6 Chava Goruarie, "The 7 biggest retail bankruptcies of 2017," The Real Deal, Dec. 15, 2017; available at: *https://therealdeal.com/2017/12/15/the-7-biggest-retail-bankruptcies-of-2017/*.

7 Alicia McElhaney, "Private Equity's Trail of Bankrupt Retailers," Institutional Investor (Oct. 26, 2017).

8 Adam Levitin, "Toys "R" Us and the Rigged Economy," Huffington Post, 09/26/2017; available at: *https://www.huffingtonpost.com/entry/toys-r-us-and-the-rigged-economy_us_59c9dbace4b0b7022a646d66*.

9 *Id*. Toys "R" Us had been making interest payments of $400 million a year on its debt.

10 Amazon may buy some Toys "R" Us stores but has no plans to continue using the Toys "R" Us brand, according to some reports. Matthew Townsend, Lauren Coleman-Lochner, Spencer Soper, "Amazon Has Considered Buying Some Toys "R" Us Stores," Bloomberg (Mar. 20, 2018); available at: *https://www.bloomberg.com/news/articles/2018-03-19/amazon-is-said-to-have-mulled-acquiring-some-toys-r-us-stores*. Abha Bhattarai, "Toys R Us liquidation sales are in full swing. Here's what to know before you shop," Washington Post, Mar. 22, 2018; available at: *https://www.washingtonpost.com/news/business/wp/2018/03/22/toys-r-us-liquidation-sales-begin-today-heres-what-to-know-before-you-shop/?utm_term=.930479b7e624*; Lauren Coleman-Lochner, Matthew Townsend, Eliza Ronalds-Hannon, "Toys 'R' Us Is Prepping to Liquidate Its U.S. Operations," Bloomberg, Mar. 8, 2018; available at: *https://www.bloomberg.com/news/articles/2018-03-08/toys-r-us-said-to-be-prepping-liquidation-of-u-s-operations*.

11 Isaac Larian, CEO of MGA Entertainment is seeking to raise $1 billion by the end of May of this year in an attempt to win bankruptcy court approval to purchase about 400 of the remaining 735 US stores that Toys "R" Us retains and the Toy "R" Us brand. Larian and two other investors have already pledged $200 million of their own money towards the purchase. Chris Isidore, "Billionaire CEO on a mission to save Toys 'R' Us," CNN Money (Mar. 22, 2018); available at: *http://money.cnn.com/2018/03/22/news/companies/save-toys-r-us/index.html*.

12 KKR & Co. L.P. Form 10-K December 31, 2017 (hereafter KKR Form 10-K) at 22. KKR states that some of the ways it invests in "distressed companies" is by investing in post-restructuring equity, "control-oriented opportunities, rescue financing," debtor-in-possession or exit financing." KKR Credit Advisors (U.S.) LLC Form ADV Part II at 55 states its use of purchasing credit default swaps.

13 Kohlberg Kravis Roberts & Co. L.P. (KKR) is a publicly traded limited partnership with a class of equity securities registered under the Securities and Exchange Act of 1934 ('34 Act). The '34 Act, among

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other things, requires that public companies file periodic reports including Form 10-Q, quarterly reports, and Form 10-K, an annual report.

14 Distressed Mergers and Acquisitions, Wachtell, Lipton, Rosen & Katz, 1 (2018) (hereafter Distressed M&A); available at: *http://www.wlrk.com/files/2018/DistressedMergers_Acquisitions.pdf*.

15 *Id*.

16 *Id*. at 2.

17 Eric Lopez Schnabel, Buying a Troubled Business: Bankruptcy and Other Options, Private Equity Focus, Dorsey & Whitney LLP, 2 (June 26, 2008) (hereafter Buying a Troubled Business).

18 Distressed M&A at 2.

19 *Id*.

20 *Id*.

21 *Id*.

22 *Id*.

23 *Id*.

24 The Art of Distressed M&A: Buying, Selling, and Financing Troubled and Insolvent Companies (hereafter The Art of Distressed M&A), H. Peter Nesvold, Jeffrey Anapolsky, Alexandra Reed Lajoux, 377, 397 (2011); Distressed M&A at 122.

25 KKR Form 10-K at 22.

26 *Id.*

27 *Id.*

28 Peter S. Kaufman, Henry F. Owsley, Distressed Investment Banking: To the Abyss and Back, 45 (2005) (hereafter Distressed Investment Banking).

29 *https://www.nasdaq.com/investing/glossary/d/debtor-in-possession-financing*.

30 *Id.*

31 The Art of Distressed M&A at 397.

32 Seward & Kissel LLP, Client Update, Distressed Investing and Bankruptcy, 4 (Jan. 15, 2008) (hereafter Distressed Investing and Bankruptcy).

33 *Id.* at 5.

34 *Id.* at 5

35 Sean A. O'Neal, "Buying Debt and Taking Control of Distressed Companies," 4 Pratt's J. Bankr. L. 499 (2008) (hereafter Buying Debt and Taking Control); Cynthia Futter and Anne E. Wells, "What to Expect from Hedge Funds Today and In the Future: An Overview and Insolvency Perspective," 29 California Bankruptcy Journal 213, 216 (2007) (hereafter Futter-Wells).

36 United States Bankruptcy Code, 11 United States Code Chapter 11, Reorganization; available at *https://www.law.cornell.edu/uscode/text/11/chapter-11*.

37 Buying Debt and Taking Control at 500.

38 Jamie Mason, "Reluctant Proprietors," The Deal, 40 (Oct. 18, 2010); available at *http://www.halseylane.com/media/news/docs/The-Deal-Oct-18-issue.pdf*.

39 *Id.*

40 *Id.*

41 Jonathan S. Henes, Esq., Kirk A. Radke, Esq., and Christopher T. Greco, Esq., "Debt is the New Equity: How Private Equity Funds Will Sponsor Buyouts Through Chapter 11," Bankruptcy Structure Insights, 14 (Summer 2009) (hereafter Debt is the New Equity).

42 Michelle M. Harner, "Activist Distressed Debtholders: The New Barbarians at the Gate?," 89 Wash. U. L. Rev. 155, 168 (2011); available at: *http://openscholarship.wustl.edu/law_lawreview/vol89/iss1/4*.

43 Distressed Investing and Bankruptcy at 5.

44 11 U.S.C. §1126(c). Distressed M&A at 125.

45 *Id*. at 5.

46 *Id*. at 5.

47 *Id*. at 6.

48 Douglas P. Bartner, Susan A. Fennessey, Financially Distressed Companies Answer Book 2013, Practicing Law Institute, 106 (2013) (hereafter Distressed Companies Answer Book).

49 *Id*.

50 Buying Debt and Taking Control at 499, 501.

51 11 U.S.C. § 364(d).

52 *Id*.

53 *Id*.

54 Distressed Investing and Bankruptcy at 5.

55 Buying Debt and Taking Control at 501.

56 *Id*.

57 *Id*.

58 *Id*.

59 *Id*.

60 *Id*.

61 *Id*.

[62] *Id.*
[63] Buying a Troubled Business at 2.
[64] *Id.*
[65] Distressed Investing and Bankruptcy at 4.
[66] The Art of Distressed M&A at 381; Buying a Troubled Business at 5.
[67] The Art of Distressed M&A at 381.
[68] *Id.*
[69] *Id.*
[70] *Id.*
[71] Distressed Investing and Bankruptcy at 5.
[72] *Id.*
[73] *Id.*
[74] *Id.*
[75] *Id.*
[76] *Id.* at 6.
[77] *Id.*
[78] *Id.*
[79] *Id.*
[80] Debt is the New Equity at 11.
[81] *Id.* at 12.
[82] 11 U.S.C. §1129(a)(10), §1129(b).
[83] See Distressed M&A at 127.
[84] *Id.*
[85] *Id.* at 112.
[86] *Id.*
[87] Stephen G. Moyer, Distressed Debt Analysis: Strategies for Speculative Investors, 266 (2005) (Discussion of disputes over valuation in bankruptcy); The Art of Distressed M&A at 306.
[88] The Art of Distressed M&A at 306.
[89] *Id.*
[90] Distressed M&A at 195.
[91] *Id.* at 310; Douglas G. Baird & Donald S. Bernstein, "Absolute Priority, Valuation Uncertainty, and the Reorganization Bargain," 115 Yale Law Journal 1930, 1952–60 (2006) (explanation of the different methods of valuation in Chapter 11 and subjective determinations and uncertainty involved in these methods)
[92] Douglas G. Baird, Bankruptcy's Quiet Revolution Coase-Sandor Working Paper Series in Law and Economics No. 755, 4 (2016).
[93] *Id.*
[94] *Id.*
[95] Futter-Wells at 7.
[96] Distressed M&A at 195.
[97] *Id.*
[98] *Id.*
[99] Distressed M&A at 192.
[100] Distressed Companies Answer Book at 27.
[101] Distressed M&A at 192.
[102] *Id.* at 193.
[103] *Id.* at 193.
[104] *Id.* at 193.
[105] Distressed Companies Answer Book at 29.
[106] *Id.*
[107] *Id.*
[108] Distressed M&A at 19.
[109] Distressed M&A at 19; Morrison & Foerster LLP, frequently asked questions about PIPEs, 1 (2017); available at *https://media2.mofo.com/documents/faqspipes.pdf*.
[110] Distressed M&A at 19
[111] *Id.*
[112] *Id.*
[113] KKR Credit Advisors (U.S.) LLC, Part 2A of Form ADV: Firm Brochure, June 9, 2017 (hereafter KKR Form ADV) at 55.
[114] *Id.*
[115] Michael Greenberger, A Look At Wall Street's Shadow Market How Some Arcane Wall Street, Financial Instruments Magnified Economic Crisis, 60 Minutes, Oct. 5, 2008, at 2, available at *http://www.cbsnews.com/stories/2008/10/05/60minutes/main4502454.shtml*.
[116] KKR Form ADV at 55.
[117] See Distressed Investment Banking at 15.
[118] Distressed Companies Answer Book at 203.
[119] *Id.* at 204.
[120] *Id.*
[121] *Id.*
[122] *Id.*
[123] *Id.* at 212.
[124] Distressed Investment Banking at 22.
[125] *Id.* at 25.
[126] *Id.* at 18.

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[127] *Id.*

[128] *Id.* at 32.

[129] Distressed M&A at 54.

[130] *Id.*

[131] *Id.*

[132] *Id.* at 54, 55.

[133] *Id.* at 57.

[134] *Id.* at 55.

[135] Distressed M&A at 55; For instance, in the case *In re Pioneer Finance Corp.*, the court held that the prepackaged plan solicitation did not qualify under §1126(b) of the US Bankruptcy Code since the solicitation process only concerned the record holders and not the beneficial bondholders. 246 B.R. 626, (Bankr. D. Nev. 2000).

[136] Distressed M&A at 57.

[137] Distressed Companies Answer Book at 217; Distressed M&A at 58.

[138] Distressed Companies Answer Book at 217.

[139] *Id.*

[140] *Id.*

[141] *Id.*

[142] Morris J. Massel, How To Negotiate A Ch. 11 Plan Support Agreement, Law360, 2 (Oct. 16, 2013).

[143] *Id.*

[144] *Id.*

[145] *Id.*

[146] *Id.*

[147] *Id.*

[148] *Id.*

[149] *Id.*

[150] *Id.*

[151] *Id.*

[152] *Id.*

[153] *Id.*

[154] *Id.* at 2, 3.

[155] A purchase price holdback is a provision that provides a holdback of a portion of the purchase price to protect the purchaser from harm due to the seller breaching its representations and warranties, covenants or other specified contingencies. The portion held back will be paid to the seller at a later date subject to the terms and conditions of the agreement.

[156] Distressed Investing and Bankruptcy at 2.

[157] *Id.*

[158] Distressed Investment Banking at 96.

[159] Distressed Companies Answer Book at 244.

[160] *Id.* at 244.

[161] *Id.*

[162] Distressed M&A at 11, 12.

[163] Bridgeport Holdings, Inc. Liquidating Tr. v. Boyer, 388 B.R. 548, 553-58 (Bankr. D. Del. 2008).

[164] *Id.*

[165] *Id.* at 558.

[166] *Id.*

[167] *Id.*

[168] Distressed M&A at 15.

[169] *Id.*

[170] *Id.*

[171] Distressed M&A at 15; Sections 141(e) and 172 of the Delaware General Corporation Law provide that a director of any company may rely in good faith on reports of the company's officers or experts that were selected with reasonable care; provided that the matter or matters are reasonably believed to be with the competence of the expert or professional.

[172] Distressed Companies Answer Book at 26, 27.

[173] *Id.* at 27

[174] *Id.*

[175] *Id.*

[176] 11 U.S.C. § 510(c)

[177] Distressed M&A at 26.

[178] *Id.*

[179] Distressed Companies Answer Book at 211, 213.

[180] *Id.*

[181] *Id.*

[182] *Id.*

[183] Distressed Investing and Bankruptcy at 3.

[184] Distressed Companies Answer Book at 206, 212.

[185] *Id.*

[186] 11 U.S.C. § 1145.

[187] 11 U.S.C. § 1145; Distressed M&A at 155.

[188] Distressed M&A at 217.

[189] *Id.*

[190] *Id.*

[191] Distressed M&A at 218.

[192] Distressed M&A at 218; See Zanett Lombardier, Ltd. v. Maslow, 815 N.Y.S.2d 547, 547 (N.Y. App. Div. 2006).

[193] Distressed M&A at 218; See Pharos Capital Partners v. Deloitte & Touche, 535 F. 522 (6th Cir. 2013).

[194] Distressed M&A at 219.

[195] Distressed Investing and Bankruptcy at 3.

[196] *Id.* at 1.

[197] *Id.*

[198] *Id.*

[199] *Id.* at 2.

[200] *Id.*

[201] *Id.* at 3.

[202] *Id.* at 3.

[203] *Id.* at 1.

[204] 26 U.S.C. § 61(a)(12); See 26 U.S.C. § 111(a), (c); Distressed Companies Answer Book at 298.

[205] Distressed Companies Answer Book at 299; 26 U.S.C. §108(a)(1)(B); 26 U.S.C. §108(d)(3).

[206] Distressed Companies Answer Book at 299.

[207] Distressed Companies Answer Book at 299; 26 U.S.C. §108(a)(1)(A) & (d)(2).

[208] Distressed Investment Banking at 49.

[209] *Id.* at 49, 50.

[210] Distressed Investment Banking at 50; Distressed Investing and Bankruptcy at 3.

[211] Distressed Investing and Bankruptcy at 3.

[212] *Id.*

[213] *Id.*

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