



*Twenty-Third Annual*

## Distressed Investing 2016

**Maximizing Profits in the Distressed Debt Market**

**Fluctuating Valuation in Chapter 11:  
Managing Expectations and Outcomes Amidst  
Changing Fulcrum Points**

**The Park Lane Hotel  
New York City  
November 28, 2016**

# **Fluctuating Valuation in Chapter 11: Managing Expectations and Outcomes Amidst Changing Fulcrum Points**

**Panel Moderator**

**Jack Butler**

**Chief Executive Officer  
Birch Lake Holdings, LP**

**Melanie L. Cyganowski**

**Member**

**and Bankruptcy Department Head  
Otterbourg, P.C.**

**William Q. Derrough**

**Managing Director & Co-Head of  
Recapitalization & Restructuring Group  
Moelis & Company**

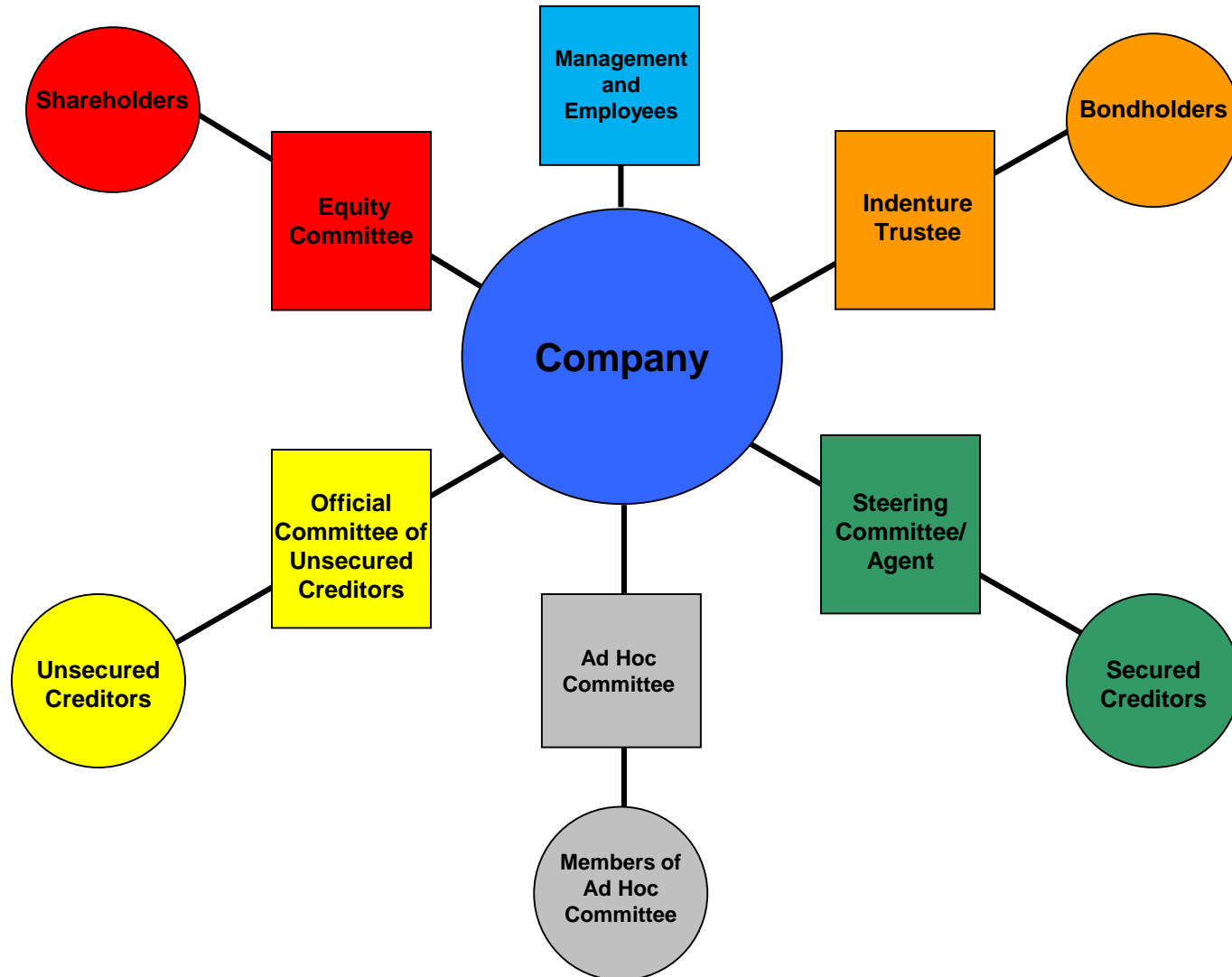
**Randall S. Eisenberg**

**Managing Director and Co-Leader  
Transformation & Restructuring Advisory  
Practice  
AlixPartners, LLP**

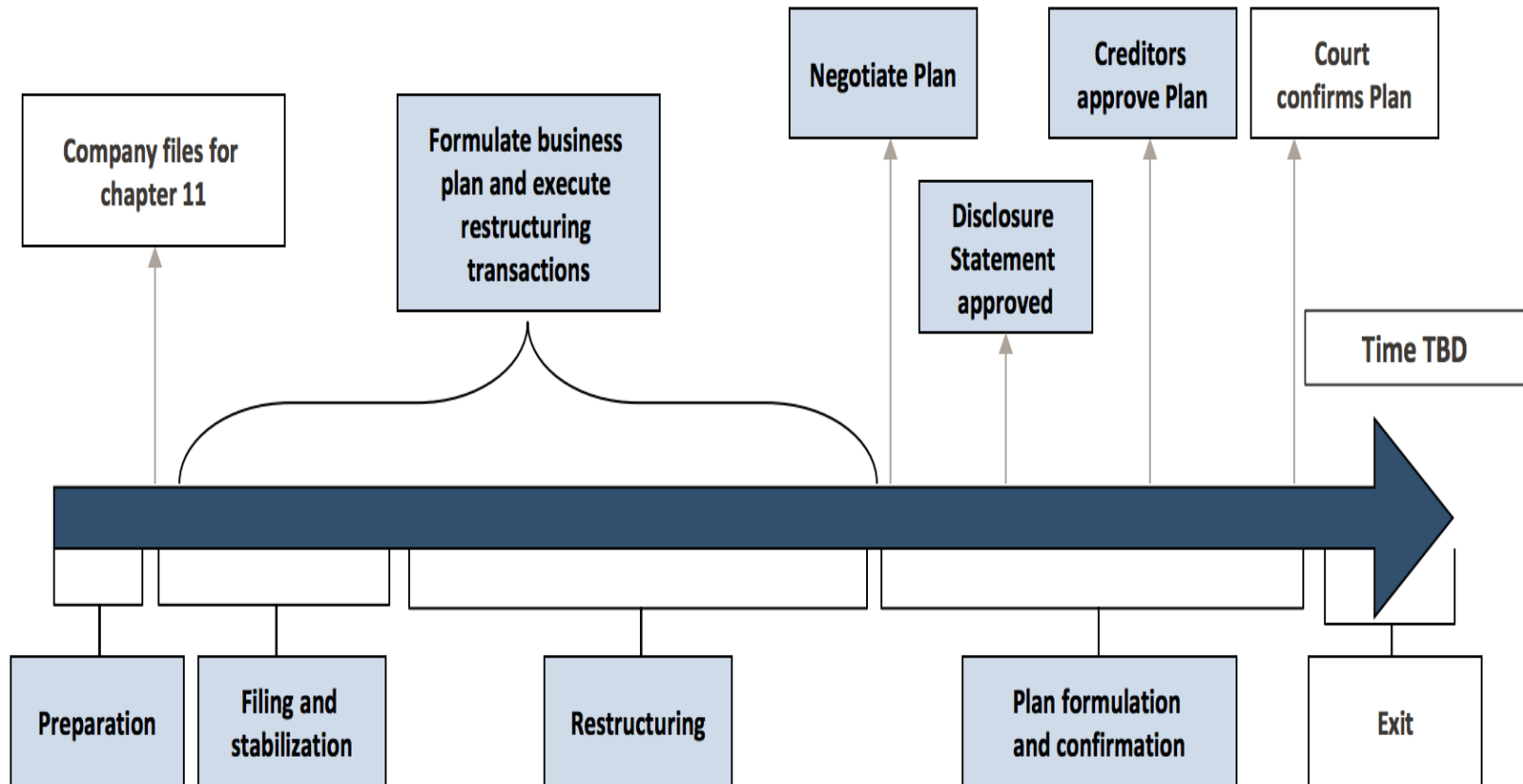
**James P. Seery, Jr.**

**Partner  
River Birch Capital, LLC**

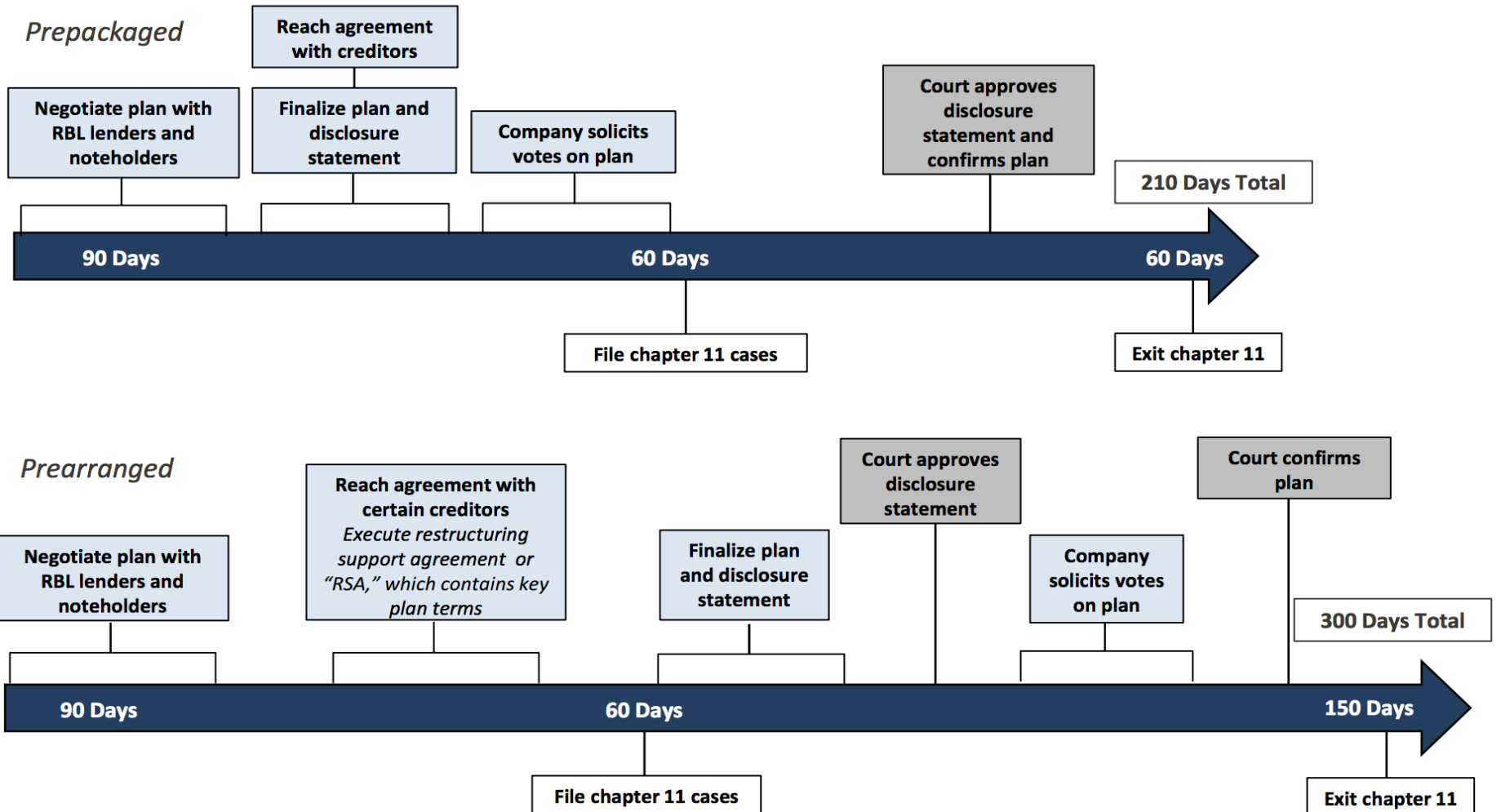
# Restructuring Stakeholders



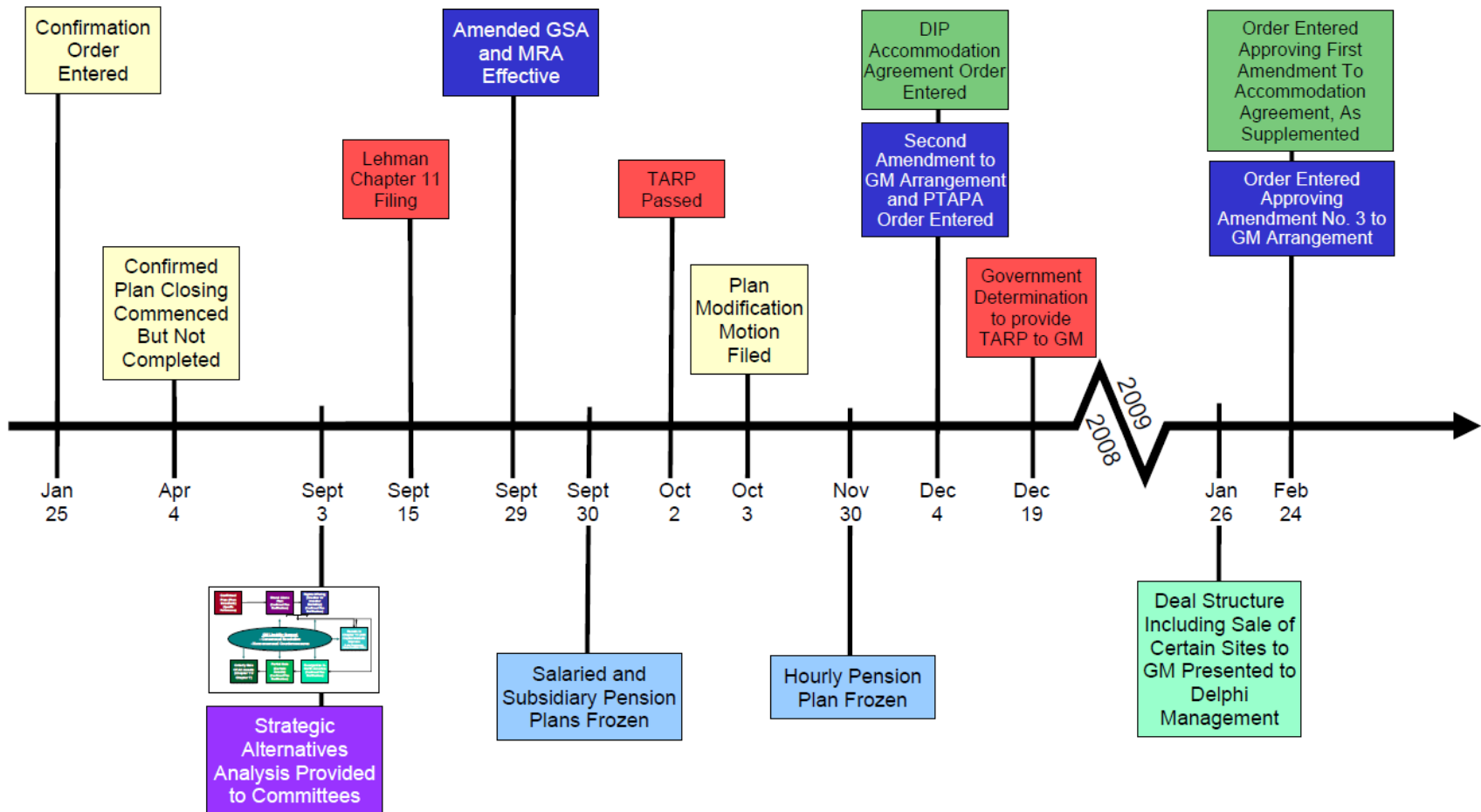
# Valuation Milestones in Chapter 11



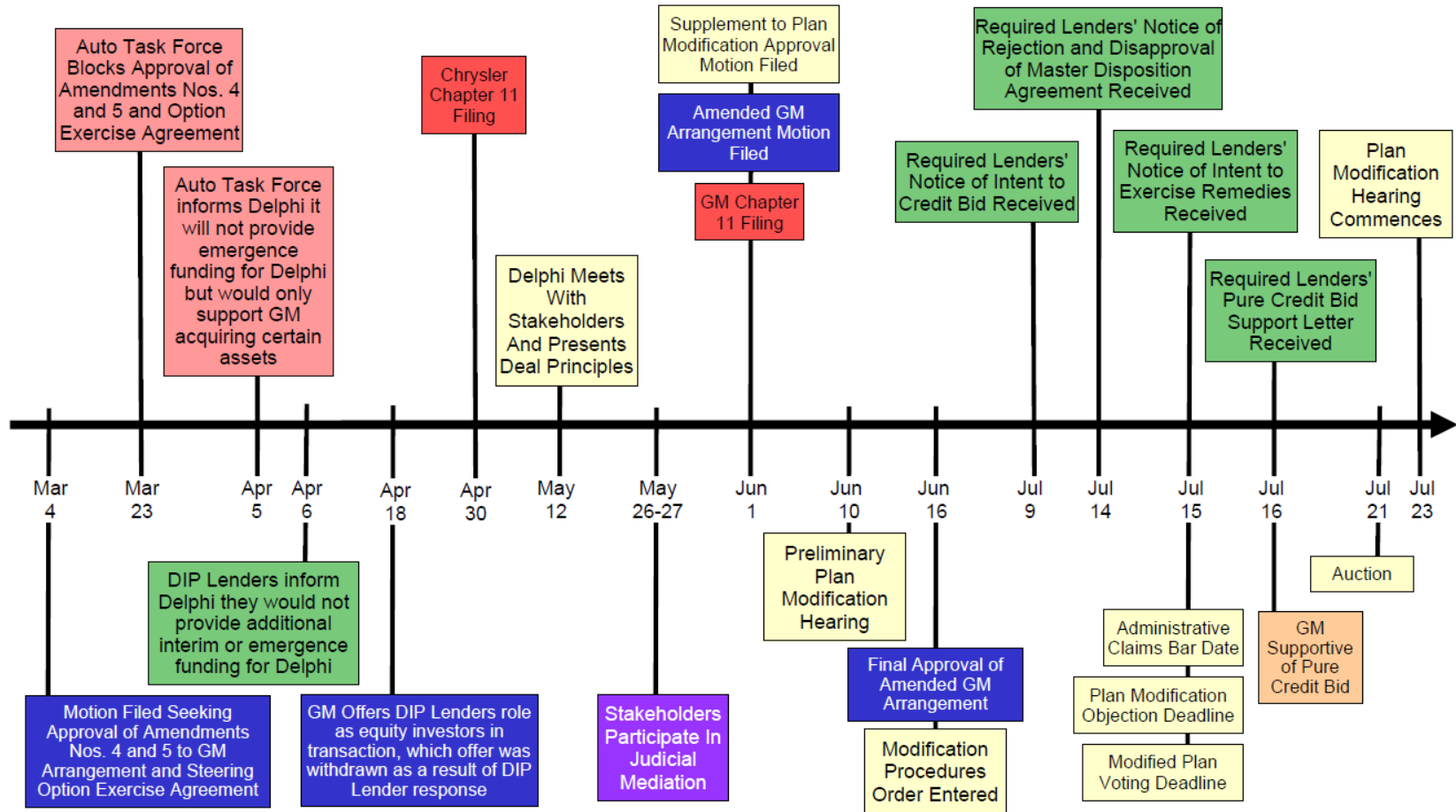
# Valuation Milestones in Chapter 11



# Delphi Corporation: 2009 Sale to DIP Lenders Yielded Max \$300 Million Distribution to Unsecured Creditors



# Delphi Sold Through Confirmed Plan Modification Process

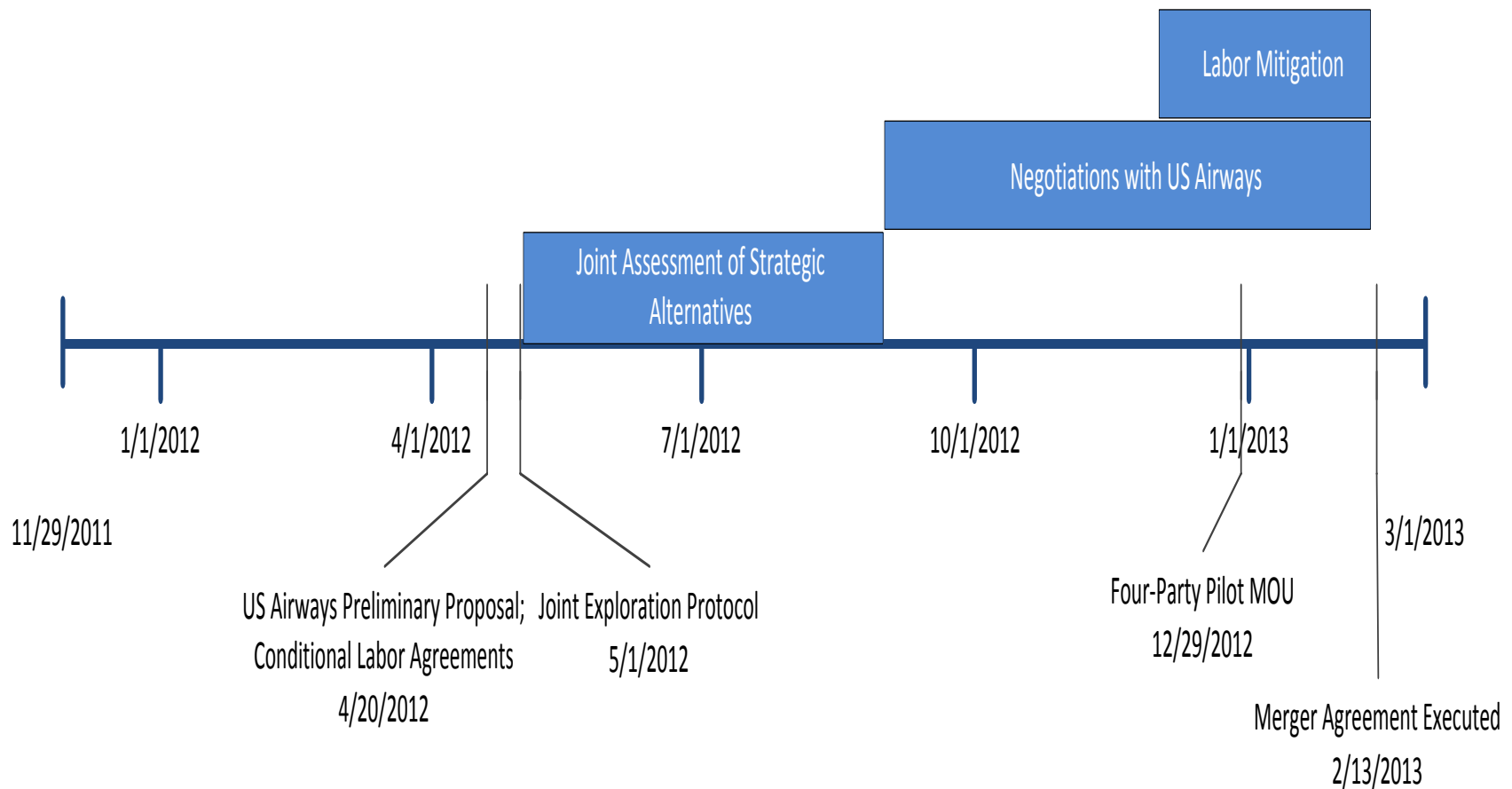


# Delphi's businesses emerged from Chapter 11 on October 6, 2009

- The entity organized by Delphi's former DIP lenders to operate its go-forward business is one of the world's largest automotive parts manufacturers and has approximately 161,000 employees, of whom around 5,000 are in the United States
- With offices worldwide, the company operates 126 wholly owned manufacturing sites, and 15 technical centers across 32 countries
- As of November 25, 2016, the company's market cap was estimated at \$18.31 billion based on a public share price of \$67.52 [NYSE:DLPH]
  - Since March 2011, the company has made distributions to its members in the form of share redemptions, repurchases and dividends in excess of \$7 billion
  - Delphi's unsecured creditors have received **no distributions to date** on their maximum distribution **of \$300 million**



# American Airlines was Merged with US Airways in a 2013 Confirmed Plan of Reorganization



# The AA / US Merger resolved AA's restructuring challenges

## Pension/OPEB

- Pension freeze carries through
- OPEB adversary proceeding continues

## Labor

- Consensual labor agreements in place; unions strongly support edMerger
- Positive management/labor relations
- Competitive compensation and benefits; career stability

## Fleet

- Combined fleet largest in industry (1511 aircraft)
- Continuing deliveries of modern, fuel efficient aircraft—saves costs and attracts customers
- Greater capacity for regional lift; improved fleet flexibility

## Network

- Expansive domestic and international networks
- Nine hubs (no closures planned)
- 682 domestic routes; 281 international routes
- Strong east coast presence
- Enhanced ability to compete against United, Delta, and other domestic and global carriers, leading to greater consumer choice

## Capital Structure

- Stronger credit profile
- Recent financings provide access to liquidity

# The AA / US Merger generated superior value for all stakeholders

## Imputed Value

- Approximately \$11 billion as of the date of the Merger Agreement, based on the trading price of US Airways common stock
- Approximately \$18 billion as of the Plan Effective Date, based on the trading price of AAL stock
- As of November 25, 2016, the company's market cap was estimated at \$24.40 billion based on a public share price of \$48.82 [NASDAQ:AAL]

## Synergies

- Over \$1 billion in annual net synergies
- \$900 million in revenue synergies from enhanced network connectivity, fleet optimization, and other factors
- Net costs savings of over \$100 million

## AMR Stakeholder Recoveries\*

- Full recoveries for general unsecured creditors
- Guaranteed distribution to holders of old equity interests; possibility of substantial additional distributions – former AMR shareholders' holdings are worth more today in AAL stock than ever before

# Selected 2016 Equity Committee Activity

Equity Committee Appointments							
Case	Bankruptcy Court	Judge	Petition Date	Equity Committee Appointment	Midpoint TEV		Status/Decision
					Debtor	Equity Committee	
<b>Cases With Equity Committees Appointed</b>							
Horsehead	District of Delaware	Judge Christopher Sontchi	2/2/2016	5/13/2016	\$280M	\$821.7M	Plan confirmed over the equity committee's objection; equity recovered nothing under plan but fee cap lifted.
Energy XXI	Southern District of Texas	Judge David Jones Judge Marvin Isgur	4/14/2016	6/17/2016	\$600M	\$3.85B	Mediation among parties failed recently, and confirmation hearing is scheduled to begin Nov. 2; plan proposes to extinguish equity interests.
Hercules Offshore	District of Delaware	Judge Kevin Carey	6/5/2016	6/21/2016	n/a	n/a	Confirmation hearing concluded, decision pending; equity committee's objection remains unresolved; post-confirmation briefs due mid-Oct.
Breitburn Energy	Southern District of New York	Judge Stuart Bernstein	5/15/2016	<i>pending</i>	\$1.625B	\$4.65B	Judge Stuart Bernstein directed the appointment of an equity committee on Oct. 14 after considering closing arguments and holding an evidentiary hearing on the matter on Oct. 11.
<b>Cases Declining to Direct Equity Committee Appointment</b>							
SFX Entertainment	District of Delaware	Judge Mary Walrath	2/1/2016	<i>denied</i>	n/a	n/a	Sept. 29 hearing saw no formal evidence admitted; Judge Walrath found valuation not a "close question."
SunEdison	Southern District of New York	Judge Stuart Bernstein	4/21/2016	<i>denied</i>	n/a	n/a	Appointment denied on Aug. 12 after a mid-July evidentiary trial; Judge Bernstein's decision rejects use of book value in valuation inquiry.
Sandridge Energy	Southern District of Texas	Judge David Jones	5/16/2016	<i>denied</i>	\$1.287B	\$2.7B - \$5.9B	Appointment denied after Aug. 1 evidentiary hearing; notable for Judge Jones' inclusion of a "practical fifth" factor.
<b>Cases With Withdrawn Requests to Appoint Equity Committee</b>							
Ultra Petroleum	Southern District of Texas	Judge Marvin Isgur	4/29/2016	<i>withdrawn</i>	n/a	n/a	U.S. Trustee declined to appoint an equity committee in late June; ad hoc equity committee is funding its own expenses; case is ongoing.
Penn Virginia	Eastern District of Virginia	Judge Keith Phillips	5/12/2016	<i>withdrawn</i>	\$241M	n/a	Request withdrawn after ad hoc equity group reached a settlement providing its professionals with a \$195,000 "substantial contribution" claim.

# Bankruptcy Commission Query

- Do the Code's provisions governing adequate protection and allocation of value still work in today's economic environment?
- If not, what has changed?

# Foreclosure Value for Adequate Protection

“[T]he Commission’s decision to use foreclosure value is an integral part of the delicate balance the Commission struck between the rights of secured creditors, on the one hand, and the reorganizational objectives of the estate, on the other hand. *Specifically, the Commission agreed that the foreclosure value of an interest should be used early in the case when determining adequate protection issues, but that the secured creditor should be entitled to receive the reorganization value of its interest in the debtor’s property through the claims allowance and distribution process later in the case.*”

# Foreclosure Value for Adequate Protection

*“[T]he term ‘foreclosure value’ means the net value that a secured creditor would realize upon a hypothetical, commercially reasonable foreclosure sale of the secured creditor’s collateral under applicable nonbankruptcy law.”*

# Commission Recommendation on Adequate Protection

*“The amount of adequate protection required under section 361 of the Bankruptcy Code to protect a secured creditor’s interest in a debtor’s property should be determined based on the foreclosure value of the secured creditor’s collateral.”*



# Commission Recommendation on Adequate Protection

- Secured creditor could challenge adequate protection determination if circumstances or valuations change
- Even though based on foreclosure value, the secured creditor's distributions would be based on reorganization value (essentially an enterprise value concept)
- If adequate protection fails, secured creditor has right to request that collateral be sold under section 363 of Code and its section 507(b) rights, including to proceeds of avoidance actions, are preserved

# Reorganization Value for Plans and Sales

*“[T]he term ‘reorganization value’ means (i) if the debtor is reorganizing under the plan, the enterprise value attributable to the reorganized business entity, plus the net realizable value of its assets that are not included in determining the enterprise value and are subject to subsequent disposition as provided in the confirmed plan; or (ii) if the debtor is selling all or substantially all of its assets under section 363x or a chapter 11 plan, the net sale price for the enterprise plus the net realizable value of its assets that are not included in such sale and are subject to subsequent disposition as provided in the confirmed plan or as contemplated at the time of the section 363x sale.”*

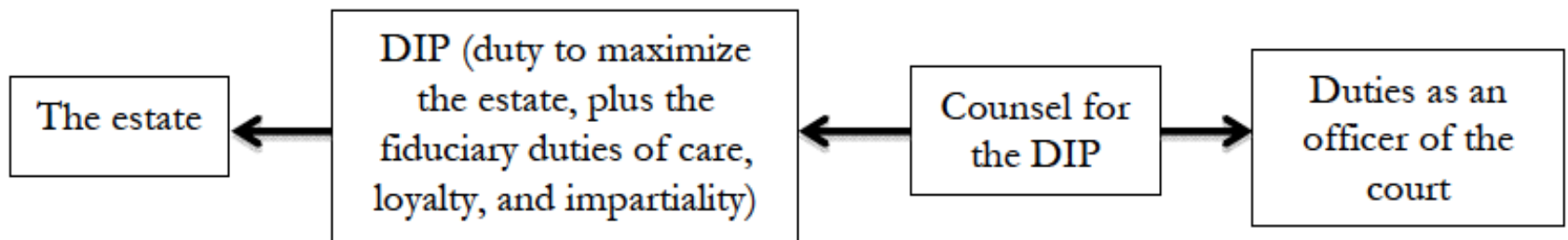
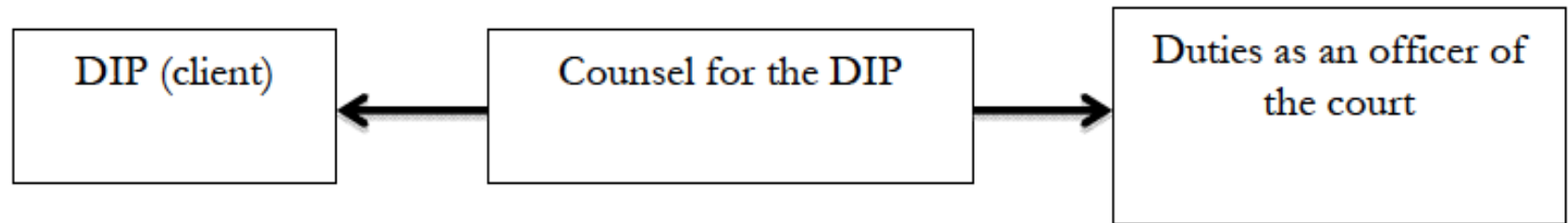
# Commission Recommendation on Redemption Option Value

- In general, “*redemption option value*” (ROV), if any, is value available to the class of creditors immediately junior to the fulcrum security based on a valuation formula that considers, among other things, the recovery by the senior (i.e., fulcrum) class and the value of the debtor during the redemption period (i.e., three years from the petition date).
- In calculating ROV, the senior class must receive the full face amount of its claims, including any unsecured deficiency claim, plus any interest at the non-default contract rate plus allowable fees and expenses unpaid by the debtor.
- Basic concept is to account for value fluctuations based solely on the timing of the valuation-realization event in the case.

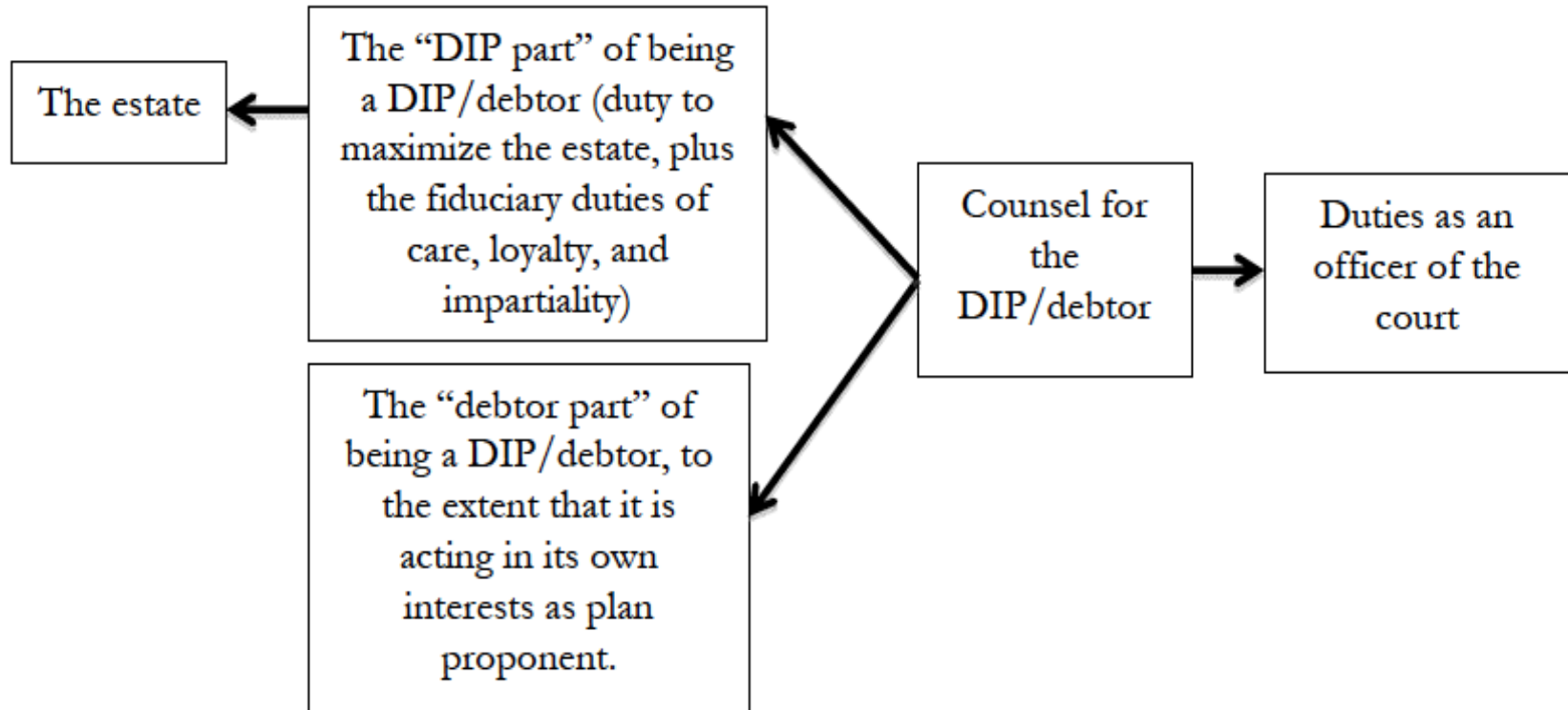
# Duties of Counsel to DIP as Fiduciary

- Counsel for Debtor versus Counsel for “Estate”
- Duties of Loyalty, Care, Impartiality
- Complexity stems from shifting nature of relationship between and among DIP, the estate, other parties in interest
- Case law and best practice presents an evolving view of where counsel fits

# Duties of Counsel to DIP as Fiduciary



# Duties of Counsel to DIP as Fiduciary



# Managing Interactions With The Company and Company Management

- Interactions with a company in financial distress and its management in the months leading up to or during a chapter 11 filing can give rise to conflicts of interest that could disqualify counsel from service as a chapter 11 debtor's counsel
- When management of a distressed company reaches out to counsel soliciting advice about its options questions relating to the compensation, duties, and retention of management are inevitable, in terms of continued employment, personal liability, insurance coverage, incentive compensation, tax matters, and similar issues
- As fiduciaries, management's focus should be, and most often is, on what is best for the company and its stakeholders

# Managing Interactions With The Company and Company Management

- While company's counsel can appropriately discuss issues of concern with management, it must navigate the discussion carefully and avoid crossing the line from providing advice to the company with respect to management issues to providing direct legal advice to individual members
- One way to fail the "adverse representation" prong of section 327 of the Bankruptcy Code would be to develop an attorney-client relationship with a member of management prior to a chapter 11 filing -- effort should be made to ensure that prepetition interactions with management cannot subsequently be construed, through the prism of hindsight, to have created such a relationship of management





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