

In a down economy Chapter 11 can solve problems

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The United States economy may not, by definition, be in a recession but it is dangerously close. Many economists do not believe near term prospects for the economy are strong and in fact, many expect a prolonged slowdown. A recent Turnaround Management Association poll of members reflects that 70 percent of turnaround professionals expect a surge of corporate debt defaults over the next three years. One option for companies suffering from economic problems, but which have sustainable long term prospects, is Chapter 11 of the United States Bankruptcy Code.

A case filed under Chapter 11 is commonly referred to as a reorganization bankruptcy, as opposed to a Chapter 7 bankruptcy which is a liquidation overseen by a bankruptcy trustee. When a business reorganizes under Chapter 11 and management remains in control, it is typically referred to as a debtor-in-possession case, which allows the owner of the business to continue running the business while attempting to reorganize. Upon the filing of the bankruptcy case, an injunction or an automatic stay is imposed which protects the business from any ongoing debt collection activity, foreclosures, enforcement of judgments or other action taken by creditors. The automatic stay is of course one of the greatest privileges of Chapter 11 and gives the debtor breathing room to propose and seek approval of a plan to repay creditors ("Chapter 11 Plan"). The Chapter 11

Plan is the contract which governs the prospective relationship between the debtor and its creditors. Creditors are placed in different classes and payment terms for each class are provided for in the Chapter 11 Plan.

One of the strongest benefits available to a business in Chapter 11 is the ability to terminate unexpired contracts or leases which are no longer economically

consensual resolution.

Another option for businesses with relatively few creditors is a prepackaged bankruptcy plan. A "pre-pak" bankruptcy plan allows the business to solicit acceptances of its plan prior to filing for Chapter 11. This can result in significant cost savings and can provide a speedy exit from Bankruptcy Court.

There are, of course, risks associated with filing Chapter 11 bankruptcy, including the possibility of creditors who do not agree to the terms of the Chapter 11 plan or who do not believe that the management team can effectively run the business. These creditors can seek to have a trustee appointed to take control of the business or even request a Bankruptcy Court auction sale of the business. If the court approves the appointment of a trustee, the trustee will be responsible for management of the debtor's business and existing management is removed. If the Bankruptcy Court approves an auction sale, the creditors may receive payment, however the business owners may receive no part of the sale proceeds.

Despite some risks associated with Chapter 11, it may be an alternative worth looking into for a viable business suffering from the harsh, but temporary, effects of a down economy.

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viable or viewed as essential to the business. For example, a debtor with retail stores can terminate the unexpired leases of store locations which are no longer profitable. This powerful tool brings landlords to the negotiating table and creates the opportunity for a

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