Analysis of Board Members' Responses to Survey and Recommended Changes for Chapter 11

Good Aspects of Chapter 11

1. Chapter 11 provides:

   - Through the plan process tremendous flexibility in creating solutions for the various parties in interest. In practice, this places a great deal of emphasis on obtaining consensus among the parties to create a confirmable Plan with a maximum number of consenting parties.
   - Through a prepackaged or pre-arranged filing an opportunity to utilize the automatic stay and the ability to transfer assets free and clear of encumbrances to create relatively economical restructurings of complex enterprises.
   - Either through DIP financing or new credit terms with vendors, or a combination of both, access to financing that was usually unavailable prior to filing which enables them to operate the business and hopefully, increase recoveries for all creditors.
   - "Highest and Best" offer concept when evaluating bids in a 363 sale allows economic value to be placed on keeping intact a going concern business and preserving jobs.
   - The debtor an opportunity for a fresh start.
   - A structure around which to frame discussion.
   - The ability to assume or reject executory contracts.
   - The ability to cure and reinstate debts.
   - A vehicle for completing a sale to a buyer who would not otherwise purchase with the burden of liabilities allowing companies to remain a going concern and save jobs.
   - Adequate protection to the creditor for the debtor to use collateral.
   - An automatic stay granting protection to debtors from their creditors as they work to reorganize the company or maximize value to creditors in a liquidation.
   - The ability to formulate and confirm plan by debtors and creditors, to restructure the debtor's debts and thereby preserve going concern value.
   - The ability to confirm that plan over the dissent of a given class of claims or interests.
   - The ability for those opposed to the plan to have a forum in which legal reasons not to confirm a plan over their objection can be determined.

- The ability to conduct going concern sales of a debtor's assets and for such sales to be free and clear of liens and claims.
- The ability to cure and reinstate debts and to provide adequate protection for the use of collateral.
- An orderly process'
- Ability to allocate values to stakeholders.
- Finality of the process (eventually).
- Mechanism to recapture fraudulent conveyances and preference actions.
- Ability to obtain financing with super priority status.

2. Chapter 11 allows all parties in interest to have a voice in the discussions.
3. Chapter 11 allows a company to reorganize when a minority of its lenders or note holders cannot agree on a restructuring out of court
4. Historically U.S. law has given parties (debtors and creditors) an opportunity to negotiate a plan that will allow the business to continue; however, the 2005 Act limited the ability for companies to complete that process by limiting the time debtors have the exclusive right to develop an plan to an unreasonable time period.
5. Chapter 11 generally prevents "insider" deals.

Comments received about Problematic Aspects of Chapter 11 – *[These are not AIRA Positions]*

1. The influence of special interest groups to carve out special treatment—for example
   - Shortening time period to assume or reject non-residential real property leases (120 days plus one 90 day extension).
   - Administrative expense claims for goods delivered within 20 days prior to filing.
   - Requiring deposits for utilities rather than having such costs considered an administrative expense.
   - Limiting time period to confirm chapter 11 plans.
2. Plans and disclosure statements that adhere to SEC requirements rather than plain language have increased the need for expensive professionals.
3. Constraints of working in court are such that parties often try to solve problems out of court before going to the bankruptcy process, which is leaving some creditors out of the process

which is controlled by secured creditors. Often secured lenders "bully" the debtor into the plan they want.

4. The increase in cost of the process has made it unworkable—the large number of professionals the debtor has to pay for and the lack of control over the work (including litigation) that they do has made bankruptcy an irrelevant tool for many companies to restructure.

5. While the need for an Unsecured Creditors Committee to have representation is clear, its role should be tailored to the nature of the case with a common sense approach, with some greater degree of uniformity among courts.

6. It is difficult to craft acceptable compensation arrangements for key debtor personnel that make significant contributions to the preservation and reorganization of the business. While essential to preserving value in the estate for all constituents, these employees are often compensated at lower rights than prior to filing as incentive and other bonus programs that existed prior to filing are no longer available. Additionally, in a sale situation, many of these positions are likely to be filled by existing personnel of the Purchaser.

7. Bankruptcy continues to be time consuming and incredibly expensive if a clear consensus on direction and methodology of execution is not established early in the case. Crowded court calendars and a bias toward forcing consensual resolution (even if it's at the lowest common denominator) by delaying controversial decisions extend the duration and expense associated with the process.

8. Retention of ordinary course professionals can be overly complicated, which makes the process expensive.

9. Current law allows "squeaky wheel" to control process, especially, if creditor has large claim.

10. Too short time period to assume or reject leases.

11. Retention and review process is not efficient.

12. In 363 sales process, cash left in business is often not adequate enough to confirm a plan.

13. Claims process is inefficient.

14. Limiting exclusivity to debtor file plan is good idea, but current terms are too short. Limitation has prevented reorganizations resulting in sales or liquidations.

15. Too much influence by secured creditors—often results in liquidation with unsecured and second lien creditors left with nothing.

16. Retention of ordinary course professionals can be overly complicated, which makes the process expensive.

Recommendations

1. Repeal changes made in 2005 Act to time period for lease assumption and give bankruptcy judges authority to control time period. While landlords were once the victims of debtor friendly practices, the pendulum may have now swung too far in their favor. The shortened period for making real estate decisions places undue burdens on some debtors, particularly for retailers, and may prohibit some otherwise successful reorganizations.

2. Raise threshold increments to record time to 15 minutes or 30 minutes to reduce administrative time and expenses for financial professionals.

3. Plans and disclosure statements that adhere to SEC requirements rather than plan language have increased the need for expensive professionals and reduced the ability of creditors and other interested parties to understand the terms of the plan including the value of the distributions. Rewrite Subchapter II of Chapter 11 Reorganization of the Bankruptcy Code to stress that plans and disclosure statements should be written in plain language clearly indicating the value of the recovery being received by both creditors and prior equity holders. (For example in one case members of the creditors committee were given a simple chart prepared by the debtor and its advisors that showed the various classes of creditors and their percent recovery based on the value of the entity. This schedule was replaced by a legal document that was almost impossible for creditors to determine their recovery, especially in relationship to the value of the recovery of other classes.)

4. Adopt the provisions of section 1111 of the Bankruptcy Code applicable to chapter 11 cases for chapter 7 cases regarding when a proof of claims must be filed. Requiring a proof of claims from each creditor when there are no objections to the amount scheduled is expensive and reduces recovery to all unsecured creditors.

5. Repeal 2005 Act changes that provided for administrative expense status for goods delivered within 30 days prior to filing. If not repealed, provide more flexibility in the payment for these 503(b)(9) claims. For example, payment could be extended to confirmation or the effective date of the plan. In some situations where the debtor does not have the ability make such payments, the debtor or buyer negotiates a payment period but the claimants have to agree to such.

6. When a company is operating in Chapter 11, a primary responsibility of management is to maintain and grow the company's value for the benefit of its stakeholders. A company that is well-managed benefits its creditors, employees, retirees, unions and the communities where they work. Companies that fail to successfully reorganize in Chapter 11 are liquidated, and creditors receive pennies on the dollar while employees see their jobs and retirement savings destroyed. When companies enter Chapter 11, it is critical that they attract and retain top

management talent. But Chapter 11 is also the most difficult time to attract and retain such talent. Managers of Chapter 11 companies are faced with intense scrutiny, stress, insecurity and an enormously complex process to navigate. They also are not provided with equity compensation programs that are available from non-Chapter 11 companies.

After the 2005 amendments, often the only way a Chapter 11 debtor is allowed to retain top management is by establishing an incentive plan where executives are allowed compensation for staying with the debtor, but only if specific goals approved in advance by the court are accomplished. In view the above-described importance of retaining top management talent, changes to Chapter 11 are needed that would loosen restrictions on Key Employee Retention Programs. Although these programs were subject to a lot of abuse in the past, the pendulum has swung too far in the opposite direction. The requirement that there must be an offer from a third party defeats the purpose of a KERP, as the employees most needed to support the estate are forced to seek out new positions. While the weak employment market has insulated estates from the impact in recent years, the brain drain from bankrupt companies is likely to become acute should the market improve. In addition, individual inequities are frequent as parties in interest benefit from the efforts of key employees that are not fairly compensated for their contributions. A debtor must use proper business judgment in formulating the program, and the court must find the program to be reasonable and fair. Creditors have the right to object to proposed KERPs, and judges are presented with a full evidentiary record upon which to make a determination. If a KERP is not appropriate or if it is not in the best interest of the company's creditors, the judge can refuse to approve it.