

## Workouts keep debts out of court, public eye

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By ANNEMARIE FRANCYK

A Chapter 11 reorganization filing can offer a private business relief from excessive debt or a sudden downturn. The federal safe haven from creditors allows the company to continue working while paring operations, negotiating payments to suppliers and lenders and saving jobs.

But at what cost?

A trip through U.S. Bankruptcy Court is an expensive one, and not solely because of the fees due to attorneys and the court. The public scrutiny that comes with a bankruptcy filing could cost the business a few dings in its reputation.

That could be what's prompting private businesses facing serious financial problems to avoid bankruptcy court altogether and opt for workouts. The out-of-court restructuring option is generally much less expensive than a formal bankruptcy, and negotiated between debtors and creditors out of the public's glare.

In a workout, a private company renegotiates loan payments and modifies contracts with two or more creditors, who could agree to accept less money for their claims or agree to an extension of the payment timeline. Under a workout agreement, the company achieves the same results as a bankruptcy - discharge from all debts or a portion of them - without the stigma.

William Brown, a Phillips Lytle LLP partner in Buffalo who has represented lenders, primarily, in these cases across the country, says workouts are more than popular.

"Booming's the word," he says. "Not so much in Western New York, because we didn't have the big boom here."

But elsewhere, such as in Manhattan and Miami, Brown says he can walk down the street and point to businesses here and defaulted condo projects there that are renegotiating their futures outside of court.

Who's pursuing a workout is something only insiders could know, since negotiations are conducted privately and agreements generally aren't publicized. A company with reasonable trade debt but too much borrowed money could restructure the bank obligation in a workout without tipping off its trade partners or anyone else who might be interested, like the government or the media.

"If you file a bankruptcy, then trade debt becomes noticed. Now all of a sudden the taxing agencies look at you more aggressively," Brown says. "Workouts try to deal with a narrow slice."

Some high-profile workouts have become known, including the talks involving Connecticut's Foxwoods Casino, which in October was granted a reprieve by lenders on debt payments until Jan. 20, according to several published reports. The Wall Street Journal last month reported an attempt by Hilton Worldwide to cut \$5 billion off its \$20 billion in loans.

An indication of the popularity of workouts could be the relatively low number of corporate bankruptcy filings. Nationally, the number of business bankruptcies spiked to 43,546 last year, but it was the first time it reached that level in a decade, according to the American Bankruptcy Institute.

In Western New York, business bankruptcies jumped slightly to 266 last year - among the lowest annual levels since 1992, when nearly four times the businesses filed for bankruptcy, according to Institute statistics.

Raymond Fink, a Harter Secrest & Emery LLP partner in Buffalo, calls workouts "negotiated breathing room" for a company facing hard times. He has been involved in workouts representing debtors in some cases, creditors in others.

The process begins, he says, long before any creditor is contacted. First the company lawyers and internal financial staff need to assess the business and determine a strategy that likely will be supported by creditors, giving the company the break it needs to ride out the problem. That assessment determines which set of creditors to approach: lenders - those secured creditors with liens on the borrower's property - or trade partners, unsecured creditors who do business regularly with the company.

A long-term owner of a private business with financial problems might be having trouble paying secured debtors. Lenders then would be approached for relief from the company's current payment structure and some temporary loans to get it through.

The chances of such a request being granted depend on the integrity of the company's business plan. The "forebearance period" that follows is used by the borrower to sell assets, find investors or a combination of the two. Faced with a choice, Fink says, lenders would rather attempt a workout over court reorganization because of the fees associated with bankruptcy filings, which can be double those of a workout.

Typical attorney fees and court fees associated with a bankruptcy filing in Western New York can average between \$50,000 and \$250,000 for a company with revenues ranging from \$5 million to \$30 million. There are also quarterly fees, to be paid to the U.S. Trustee's Office, based on the debtor's business expenses.

A bankruptcy filing can put greater financial strain on a business already struggling with cash flow. "My own view is you shouldn't be filing Chapter 11 if you have other options," Fink says.

"Lenders, given the changes in the world markets, are more interested to sit down with borrowers and listen to what the borrower has to say," he adds. "I seldom see a lender who says no, though they may ultimately do so because the company is too far gone."

While most workouts involve secured creditors, it's not uncommon to renegotiate payment structures with trade creditors as well. A letter might propose a reduced amount of debt and a longer payback period in addition to payments for new products purchased on usual terms. In real-estate workouts, trade creditors, such as janitorial services and elevator maintenance companies, more often are kept current because they're critical to the operation of the building, Brown says.

Why would a trade partner, presumably facing its own struggles, agree to what amounts to a discount of its goods or services?

"They need the business," Brown says, and they don't want to pass off the opportunity - even at a discount - to a competitor.

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