OUTSIDE PERSPECTIVES

Coming Soon To A Bankruptcy Court Near, Or Perhaps Not-So-Near, To You

NEAL L. WOLF

In 2001, Houston-based Enron Corporation, one of the world's leading electricity, natural gas, pulp, paper, and communications companies, with claimed revenues of nearly $101 billion in 2000, the employer of approximately 22,000 individuals, and the company that had given its name to Houston's brand new baseball stadium, filed a chapter 11 case. Eschewing the United States Bankruptcy Court for the Southern District of Texas where, only a few blocks from Enron's corporate headquarters, five bankruptcy judges presided daily over chapter 11 cases, Enron chose to file its case in New York City, some 1,419 miles away.

In December of 2005, San Jose-based Calpine Corporation, the ninth-largest producer of electricity in the world, the largest producer of geothermal power in the world, and the supplier to some 23 million homes of about 3.5 percent of all electricity used in the United States, filed a chapter 11 bankruptcy case. While Calpine had operations throughout the world, most of those operations were based in the western United States. Calpine had been continuously headquartered in Northern California since its founding in the early 1980s. While three bankruptcy judges regularly presided over chapter 11 cases in San Jose, at a courthouse located less than two blocks and a two-minute drive from Calpine's corporate headquarters, and while another five judges sat in San Francisco and Oakland, less than a one-hour drive from San Jose, Calpine chose to file its case in New York City, some 2,944 miles away.

In December of last year, some 161 years after its founding, the Chicago Tribune Company, as much an icon in the City of Chicago as Mrs. O'Leary's cow and the "loveable loser" Chicago Cubs baseball team that it happens to own, also sought the protection of our nation's bankruptcy laws. Chicago's nine bankruptcy judges sit each day less than one mile from the Company's Tribune Tower headquarters. Where was the Tribune chapter 11 case filed? In Wilmington, Delaware.

The New York Times recently reported that Michael Cox, the Attorney General of Michigan, sent a letter to the CEO of General Motors, urging GM to file its anticipated chapter 11 case in Detroit. GM's response to the Attorney General's pleas was diplomatic and evasive. To the hoteliers and restaurateurs of Detroit, however, and to Detroit-area bankruptcy lawyers, it undoubtedly had a less-than-encouraging tone:

> … The filing location would be just one of many factors we would need to take into account.

The majority of large, complex chapter 11 cases are filed in New York City and Wilmington, Delaware. As *The National Law Journal* recently reported, "[s]o far this year, the U.S. Bankruptcy Court for the District of Delaware and the U.S. Bankruptcy Court for the Southern District of New York have grabbed 26, or 65%, of new bankruptcy filings for public companies with asset values of more than $252 million." The historic trend not only continues; it gains momentum. During the last economic downturn, the referenced percentage was only 57%. In 2008, these two federal judicial districts provided the "home court" for 1,379 chapter 11 bankruptcy cases, while the bankruptcy courts of Los Angeles, Chicago, Atlanta, Houston, and Miami together captured only 1,172 such cases. During the first three months of 2009, the New York and Delaware courts were home to 1,399 new chapter 11 cases, while the courts of those other large cities saw only 426 new chapter 11 filings.

What is the Explanation for this Phenomenon?

By way of background, before answering the "Why Does this Happen?" question, I should answer the "How Can this Happen?" question. The answer requires an explanation of the bankruptcy venue law. Under the venue statute, which was enacted by the Congress of the United States, a chapter 11 case may be commenced in the federal judicial district in which (1) the domicile, residence, principal place of business in the United States, or principal assets in the United States of the debtor are located, or (2) there is a previously-pending a bankruptcy case concerning such person's "affiliate." For a corpora-

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tion, limited liability company, or partnership debtor, the state of incorporation or formation qualifies as its state of domicile or residence. Moreover, an entity that directly or indirectly controls or is controlled by a debtor is an "affiliate" within the meaning of the Bankruptcy Code. Hence, an entity that is incorporated in Delaware or New York (as many companies are), is affiliated with an entity that is incorporated in Delaware or New York, or has significant assets in Delaware or New York, may file its chapter 11 case in those states.

We now turn to the far more interesting -- "Why Does this Happen?" -- question. The answer is that many, if not most, of the top debtor-representation bankruptcy attorneys in America believe that the judges, judicial staffs, United States Trustees, and Clerks of the bankruptcy courts in the Southern District of New York and District of Delaware have created a more flexible, "user-friendly" and predictable environment in which to file and prosecute such cases. While the lawyers will not admit openly to the following bias, they believe also that, by virtue of their experience in large and complex cases, the judges in these districts are better equipped from the standpoint of sophistication, knowledge and experience, to handle the cases. While the lawyers that advise their clients to commence complex cases in those districts do not know and cannot predict how every important issue in every case will be decided, those attorneys can anticipate, among other things, that [i] the courts and United States Trustee will fully co-operate in the scheduling of urgent matters on shortened notice; [ii] the courts and United States Trustee have developed and will employ case-tested and pragmatic procedural mechanisms for dealing efficiently with the large volume of motions and fee applications that are certain to be filed; [iii] debtors' counsel is not likely to be disqualified from representing all of the affiliated debtors because of the existence of inter-company claims; [iv] debtors' counsel is not likely to be disqualified from representing the debtors because of isolated conflicts of interest that can be handled separately by "conflicts counsel"; [v] certain important "first day orders," such as orders allowing the debtors immediately to pay the pre-petition claims of critical and otherwise recalcitrant suppliers of goods and services, are likely to be granted if they are within certain monetary bounds (which may not be the case in other courthouses); [vi] various "protections" commonly sought by "stalking horse" bidders for estate assets (including, among other things, "break-up fees," expense reimbursement provisions, and bid cushions) will, within certain relatively well-defined bounds, be approved (which also may not be the case in other courthouses); [vii] in a case in which it is anticipated that the debtors' business will be liquidated, the court will almost certainly allow such liquidation to occur in the chapter 11 case, rather than convert the case to a chapter 7 case, in which a chapter 7 trustee is appointed and the debtor in possession loses control of the case; and [viii] the high standard hourly rates and/or other fee arrangements of the attorneys, financial advisors, investment bankers, and other professionals that may need to be employed, when within certain well-defined bounds, will not surprise or "shock the conscience" of the United States Trustee and the bankruptcy judge.

Some would, and do, persuasively argue that these expectations reflect a "debtor bias" in these districts. It can be argued with equal persuasiveness, however, that the "expectations" listed above reflect not so much a debtor bias, as a bias in favor of a more flexible and pragmatic approach to the management of large and complex cases. One can even argue that, in some respects, this approach is not merely flexible and pragmatic, but more economic. In any event, the perceptions and expectations that created this phenomenon in the first place – perceptions of greater experience, sophistication, and facility in dealing with large and complex cases – are enhanced and further justified by each new filing in New York and Delaware. In a sense, the very fine judges in other districts, who in most instances are equally qualified and sophisticated, simply don't stand a chance to prove their mettle.

Neal L. Wolf is a partner with Butler Rubin Saltarelli & Boyd LLP, a Chicago litigation and bankruptcy boutique. He is chair of firm's Business Reorganization, Bankruptcy and Insolvency practice group. The views expressed are personal to the author.

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