VIEWPOINT

The Non-Uniform Reality Of 'Uniform' Bankruptcy Laws

By Jonathan Friedland and Bennett Spiegel

One of a series of opinion columns by bankruptcy professionals.

Many pundits are predicting that more and more troubled situations will be resolved outside of Chapter 11 in the near and intermediate term. Factors said to be driving this trend include uncertainty created by the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, the efficacy of state-law alternatives, and the growing power of hedge and private-equity funds and their desire to keep professional fees down and avoid other Chapter 11 costs.

We aren't so sure any of these factors is really that new. The BAPCPA, we think it's fair to say, is viewed by many of the Chapter 11 bench and bar alike as a negative development that makes Chapter 11 a less favorable option than it was before. However, the BAPCPA is not the first time the Bankruptcy Code has been amended in ways that have created uncertainty. Chapter 11 still provides a distressed company and its constituents unique tools and powers that are simply not available in the state-law alternatives to bankruptcy (all of which have been around for a long time) - and better practitioners have never hesitated to use these alternatives. Also, the desire to keep costs down has always been a driving force to all constituents including the banks and other players who are now often being replaced by hedge funds and private equity funds.

One aspect not addressed by the BAPCPA, and not cited by those who argue that Chapter 11 cases will give way to an increased number of out-of-court workouts, receiverships, "assignments for the benefit of creditors" and the like, but worth exploring - and which is critical to understand if a bankruptcy is inevitable - is that many practical and legal issues are addressed differently by different bankruptcy courts. This non-uniformity is not cause to avoid Chapter 11, but it is a complexity of Chapter 11 that must be understood because substantive outcomes may be driven by these differences.

Notwithstanding that Article I, Section 8 of the Constitution empowers Congress to establish "uniform laws on the subject of bankruptcies throughout the United States" (ultimately giving rise to the U.S. Bankruptcy Code, as amended), practitioners and sophisticated clients well recognize that both substantive and procedural results may differ depending on which bankruptcy court presides over the case.

This requires the venue analysis that we all speak of and that some commentators criticize as inappropriate forum shopping. This piece is not about the debate concerning the propriety of selecting a venue based on strategic issues. It is what it is: Advisers typically take advantage of the wide latitude the code gives to a company in deciding where to file for bankruptcy, by first considering which courts are available, then analyzing the practical differences of appearing in the various venues, determining what legal issues are most important, and then analyzing which bankruptcy courts (of those where venue is permissible) are most likely to rule on those issues in a manner most favorable to the debtor company, or the constituents that are pressuring the debtor to make one venue choice or another.

The practical issues which advisers assess focus on the real world realities of filing a case in a particular forum and do not turn on the non-uniformity in case law. Examples include questions such as:

How many bankruptcy judges sit in a venue? If there is only one, then picking the venue is the same as picking the judge. If there are only two and both are

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"known quantities" that may be preferable to filing in a venue where there are judges that are perceived to be unpredictable or otherwise unfavorable. In a large, multi-judge jurisdiction, how uniformly have the various Judges ruled on substantive legal issues and how uniform are the court procedures?

How well developed are the local bankruptcy rules in the potential forum? Some may view better-developed rules as an advantage giving rise to predictability and paving the way for smooth case handling. Others may prefer the Wild West-type of venue where fewer distinct local rules may be perceived as an opportunity for more creativity. In multi-judge districts, what are the local rules?

How good is access to the court? The access question may include several subordinate issues such as: How likely is the court to grant a hearing on short notice or emergency basis given the predilections of the judges and the quantity of active cases on the docket? What kind of filing system does the court have? Is it electronic or manual? How efficient and user-friendly is the court clerk's office? How difficult is it to physically get to the court if you're traveling from out of town? If the court is not in a major city, what is the breadth and depth of available local counsel?

How is the U.S. Trustee for the potential district perceived?

Potential debtors and their constituents (and their respective advisers) must also consider the non-uniformity in case law between, and sometimes among, federal circuits. What we briefly comment on here is the surprising number of legal issues that the uninitiated might expect to be well settled and uniform "black letter" law, but which in fact are anything but. These include:

- Will a request for substantive consolidation be granted?
- Will a plan provision for releases of non-debtor third parties be permitted?
- Will a sale of substantially all assets outside of a plan early in the case be achievable?
- Will a non-assignable executory contract be assumable by the debtor?
- Will the court halt suits against the debtor company's directors and officers during the chapter 11 case?

There are other issues in many cases that will have a major impact on the parties. Better practitioners try to anticipate these as well. However, not all are equally predictable because it is not usually feasible to plan for every potential permutation in a case. It is more likely than not that any particular venue will be perceived as more favorable with respect to certain important issues, and less favorable with respect to others. Accordingly, it will usually be necessary to weigh or otherwise prioritize the importance of each issue assessed in the venue analysis in order to formulate a recommendation or a list of preferred venues.

The bottom line is that while a plain reading of Article 1, Section 8 might lead one to conclude that the choice of where to file a Chapter 11 case is a trivial decision, the non-uniformity in both the practical and legal aspects of practicing in the various potential venues clearly dictates otherwise.

Happy hunting!

(Opinions expressed are those of the author or authors, not of Dow Jones Newsletters.)

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