

## Chapter 11 Bankruptcy

### Information About Filing Chapter 11 Bankruptcy

Due to the poor economy, some local businesses may be in financial trouble, suffering from the burden of past business decisions. Those same businesses, however, could operate profitably if they had relief from their existing debt. Chapter 11 Bankruptcy can provide that relief, as opposed to those businesses having to close their doors.

### How Does Chapter 11 Work?

Chapter 11 Bankruptcy is primarily designed to facilitate corporate financial reorganization, to allow businesses to continue to operate while they restructure their debt under a repayment plan. The purpose of Chapter 11 Bankruptcy is to promote otherwise viable businesses to continue to operate in order to generate revenue, protect jobs, and to allow the payment of creditors over time, as opposed to stopping operations and liquidating assets. Chapter 11 can free up capital from paying old debt in order to finance current operations. It will prevent the loss of vital assets or cash to creditors from their collection actions. It can also facilitate the rejection of burdensome leases or contracts, such as expensive facility leases or unfortunate equipment purchases. Chapter 11 reorganization can not, however, create a new market, increase gross revenue, or resolve deficiencies in the skills that are required to profitably run the business. The owners and managers of the business must be able to fix the underlying problems that brought them to Chapter 11 in the first place, in conjunction with restructuring the debt in a repayment plan.

By filing a Chapter 11, a debtor can seek a repayment agreement with all of its creditors, called the "Plan", while all or part of the business continues to operate. Under the plan, a Chapter 11 debtor can reorganize its business structure, liquidate property, reject certain burdensome contracts or properties, and modify payment terms of secured and unsecured obligations, all of which is subject to Court approval. The contents of a Chapter 11 bankruptcy repayment plan must include a classification of claims and must specify how each class of claims will be treated under the plan. In one class, the plan will provide for the repayment of loans secured by real estate, machinery and other types of property, to be paid over an extended period of time. Under certain circumstances, the interest rate on those secured loans may be adjusted under the plan. In another class, the plan will provide for the payment of any outstanding federal or state tax obligations, to be paid over an extended period of time. In another class, most plans will propose that unsecured creditors (i.e., credit lines, trade debt, loans) be paid significantly less than the full amount of their claims in full satisfaction of their claims. Finally, in typically the last class of creditors, holders of equity claims against the

Debtor will generally receive no payments or preferential treatment under the plan. Creditors whose contractual rights are to be modified or who will be paid less than the full value of their claims under the plan vote on the plan by ballot, but they do not have absolute veto powers.

### Disclosure Statement

A written disclosure statement must be filed with the Court. The filing of the disclosure statement is preliminary to the voting on the plan. The disclosure statement must contain information concerning the assets, liabilities, and business affairs of the debtor sufficient to enable a creditor to make an informed judgment about the Debtor's plan of reorganization. The Court will conduct a hearing to determine whether the information contained in the disclosure statement complies with statutory requirements, and approve same if appropriate, before the disclosure statement can be sent to creditors. After a disclosure statement has been approved by the Court, the debtor can begin to solicit creditor acceptance of the plan; creditors may also solicit rejections of the plan. Once the voting ballots have been collected and tallied, the Bankruptcy Court will conduct a confirmation hearing to determine whether to confirm the plan or dismiss the case.

### Plan Confirmation

At the confirmation hearing, the Bankruptcy Judge will review the plan, along with profit and loss statements and financial records to determine if the debtor is financially capable of adhering to the terms of the proposed plan. If the Court finds that the plan was proposed in good faith, is fair and equitable to creditors, and is in compliance with all statutory requirements, the Court will approve confirmation of the plan, by which unsecured debts are discharged and non-dischargeable debts are to be paid pursuant to the repayment terms of the plan. The Bankruptcy Court, however, may dismiss a Chapter 11 case "for cause" where there is a continuing loss to the estate, an inability to effectuate a plan, unreasonable delay that is prejudicial to creditors, or an inability to consummate a confirmed plan. If a case is dismissed, creditors are entitled to resume their collection actions against the debtor.

### Management's Duties

A Chapter 11 debtor is generally referred to as a "Debtor-In-Possession." Typically, existing management continues to run the day-to-day operation of the business, without the appointment of a case trustee. Chapter 11 requires a significant time commitment on the part of the debtor's owners and managers to fully comply with procedural obligations. Chapter 11 provides that in exchange for stopping the collection of debts by creditors and granting other bankruptcy protection rights, a debtor must provide full disclosure of its financial condition to creditors and the court, both at the beginning of the case and on a monthly basis thereafter. A debtor has what is called a "fiduciary" duty to its creditors while a Chapter 11 is pending. This means that a debtor must keep its creditors highly informed of all financial information, be extremely honest, and be protective of creditors' interests before the interests of the debtor. For example, a debtor has the duty to provide a full accounting for all its property, investigate and possibly prosecute law suits to recover preferential transfers (including payments made to insiders), examining and, where appropriate, objecting to creditors' claims, and filing monthly operating reports with the U.S. Trustee's Office. Debtors must remain up-to-date with their current debt and normal operating costs, and make quarterly compensation and reimbursement payments to the Bankruptcy Court, their attorneys, accountants, and others whose services they use, all while satisfying the terms of the repayment plan. Debtors are allowed to sell or trade certain business assets without Court authorization.

### Automatic Stay

The automatic stay provides a period of time in which all judgments, collection activities,

foreclosures, and repossessions of property are suspended and may not be pursued by creditors on any debt or claim that arose before the filing of the bankruptcy petition. The automatic stay takes place immediately upon the filing of the bankruptcy petition. The automatic stay provides the debtor with a breathing spell, during which negotiations with creditors can take place to try to resolve the inherent difficulties in the debtor's financial situation and to allow the debtor the time to formulate a repayment strategy. Creditor's Committee

Creditors' committees can play a major role in Chapter 11 cases. A creditor's committee is appointed by the U.S. Trustee's Office upon the filing of a Chapter 11 petition. The committee generally consists of unsecured creditors who hold the seven largest unsecured claims against the debtor. The committee is appointed to represent the interests of all of the unsecured creditors in the bankruptcy case. The committee may consult with the debtor, investigate the acts, conduct, assets, liabilities, financial condition, the operation of the debtor's business and the desirability of the continuance of such business, and any other matter relevant to the case. The committee may participate in the formulation of a plan, and if the debtor fails to submit one, may submit a plan of its own. Small Business Debtor

A small business is defined by the Bankruptcy Code as a person engaged in commercial or business activities that has aggregate noncontingent, liquidated, secured, and unsecured debt that do not exceed \$2,000,000.00. If a debtor qualifies, and elects to be considered a small business, the case is put on a "fast track" and treated differently than a regular Chapter 11 case. For example, the appointment of a creditors' committee and a separate hearing to approve the disclosure statement are not mandatory. Many procedural hurdles are simplified when a debtor elects a small business classification and the Debtor may proceed to confirmation much more rapidly. Speak With Us

Business owners generally tend to be independent people who may be reluctant to admit to themselves the true financial distress their business is in. It is critical that those businesses speak with a bankruptcy attorney who is well versed in both practical business matters as well as the law as soon as possible. By waiting too long to seek help, the debt obligations can become too onerous, which can doom the businesses' Chapter 11 reorganization plan. When carefully considered and adopted from the early stages of distress, a Chapter 11 can provide meaningful and tangible relief. If you are considering filing Chapter 11 Bankruptcy, the first step you should take is to speak with a knowledgeable and experienced bankruptcy attorney. The team at Tully Rinckey, PLLC has handled bankruptcy cases on behalf of businesses throughout New York. We will review your situation and help you determine if Chapter 11 bankruptcy is the right step for your business. For a consultation with an experienced bankruptcy

attorney, call our offices at 1-888-529-4543 or send an email to [info@1888Law4Life.com](mailto:info@1888Law4Life.com)

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