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# Putting the Bankruptcy Puzzle Together



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A Presentation for National Grain & Feed Association

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"Not scared yet? Just wait until I  
get to Chapter 11!"

"Laws are not abstract propositions. They are expressions of policy arising out of specific situations and addressed to the attainment of particular ends. Thus, an understanding of bankruptcy law is enhanced by an understanding of the goals it seeks to attain."



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# Bankruptcy Has Two Fundamental Goals

## Fundamental Goal #1: Fresh Start for the Debtor

The modern day Bankruptcy Code is designed to relieve the honest but unfortunate debtor of its indebtedness so that the debtor can make an economic fresh start and emerge as a viable productive entity.



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# Bankruptcy Has Two Fundamental Goals

## Fundamental Goal #2: Equitable Distribution

The Bankruptcy Code is designed to place all of the debtor's property under the control of the court for equal distribution among all creditors.



# Public Purpose

- Bankruptcy replaces individual collection remedies which have been characterized as "grab laws."
- An important function of bankruptcy law is to prevent aggressive individual creditors from starting a "run" on the debtor by assuring all creditors that they will be treated equally in bankruptcy.



# Bankruptcy Court is a Court of Equity

Unlike most courts, a Bankruptcy Court is not a court of law, it is a court of equity.

There is a BIG difference.

In a court of equity, those in “the right” don’t always prevail.



# Benefits of Bankruptcy

- First, a collective process reduces the costs associated with monitoring the debtor to protect creditors from the race to the courthouse that occurs outside the bankruptcy process.
- Second, interested parties are benefited by the administrative efficiencies of one collective proceeding.
- Third, a collective proceeding is likely to increase the aggregate pool of assets by prohibiting piecemeal liquidation of the debtor's assets.



# Right to Bankruptcy Protection

Protection in bankruptcy is not a fundamental right. There is no constitutional right to obtain a discharge of one's debts in bankruptcy. Rather, it is a statutory right for those who qualify.



# Forms of Bankruptcy Relief

- Generally, 2 Forms:
  - Liquidation
  - Reorganization
- Chapters:
  - Chapter 7 – Liquidation (Personal or Business)
  - Chapter 11 – Reorganization (Personal or Business)
  - Chapter 12 – Reorganization (Farmer)
  - Chapter 13 – Reorganization (Personal)



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# Who Qualifies For Bankruptcy Protection?

- The threshold to qualify to file for and obtain protection from bankruptcy is relatively low.
- As a general rule, those not able to pay debts as they become due qualify for bankruptcy protection.
- You DO NOT need to be “insolvent.”



# What It Means To Get a Discharge

- A discharge wipes a debt clean such that the debtor is no longer liable.
- Discharge allows the debtor to obtain its fresh start.
- There is no absolute right to a discharge unless the debtor files in good faith and adheres strictly to the Bankruptcy Code.
- Not all debts are dischargeable (i.e., fraud, taxes).



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# Who Is Entitled To A Discharge?

- Individuals - through reorganization or liquidation
- Corporations – only through reorganization, not liquidation



# Equitable Distribution – Order of Payment

- Secured Creditors
- “Priority claims”
- Unsecured Creditors
- Stockholders



# Some Have More “Priority” Than Others

- The Bankruptcy Code recognizes the importance of some debts over others.
- There are 8 different types of “priority claims” including:
  - Administrative expenses of the bankruptcy estate, such as attorneys (2<sup>nd</sup> priority)
  - Wages of employees, up to \$10,500 (4<sup>th</sup> priority)
  - Claims of persons engaged in the production or raising of grain against a debtor who owns or operates a grain storage facility (6<sup>th</sup> priority).



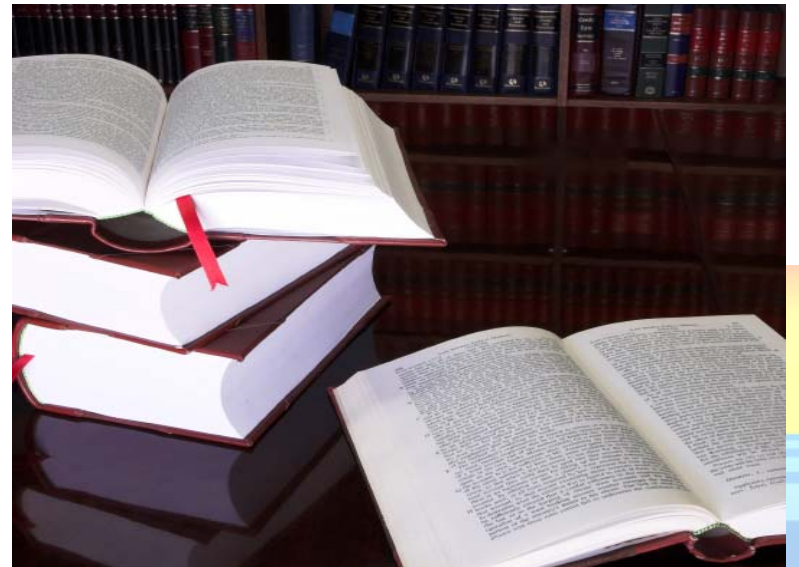
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# The Bankruptcy Code

## 11 U.S.C. §§ 101, *et seq.*

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### Relevant Provisions



# The Automatic Stay – Section 362



- Purpose:
  - ❑ Provide the Debtor with a “breathing spell” in which it can attempt to reorganize and achieve a fresh start.
  
- The Stay prevents:
  - ❑ The commencement or continuation of any action or proceeding against the Debtor.
  - ❑ The enforcement of a judgment date against the Debtor or its property.
  - ❑ Any act to obtain possession of property of the estate.
  - ❑ The unilateral termination of an executory contract with the debtor.

# Executory Contracts – Section 365



- Defined – a contract under which performance remains outstanding for both parties which failure to perform would result in a material breach of the contract.
- Executory contracts are property of the bankruptcy estate – therefore, the automatic stay prevents parties from taking terminating or adversely affecting the debtor's rights under the contract .
- This is the case despite any contract provision to the contrary.

We will come back to this!



# “Safe Harbors” for Commodities and Forward Contracts – Section 556

- Special protections for parties to “commodities and forward contracts.”
- Includes agreements for the purchase and sale of commodities for future delivery on, or subject to rules of, a contract market or board of trade, and leverage transactions.
- Gives parties to the contract a right to unilaterally terminate, liquidate or accelerate the contract on account of insolvency if the contract so provides.



## Bankruptcy of Grain Storage Facilities – Section 557

“Grain” means wheat, corn, flaxseed, grain sorghum, barley, oats, rye, soybeans, other dry edible beans, or rice.

A “grain storage facility” is a site or physical structure regularly used to store grain for producers, or store grain acquired from producers for resale.

Court may expedite the determination of interests and the disposition of grain notwithstanding other Bankruptcy Code sections, usually within 120 days of the bankruptcy.



# What is a Plan?

- A plan is the Debtor's proposal to repay creditors
- A plan must separate creditors into classes
- Creditors get to vote on the plan
- A plan does not have to be a reorganization, it may set forth a plan for liquidating the debtor's assets



# What is a Disclosure Statement?

- The disclosure statement is a document required to be filed in conjunction with a plan that provides information to creditors so that they can make a reasonably informed decision whether to vote to accept or reject the plan. In many ways, it is similar to a prospectus.
- The disclosure statement must be approved by the court prior to being sent to creditors.



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# Confirmation of a Plan

There are 13 statutory requirements that must be satisfied for the Court to confirm (approve) a plan, these include:

- ❑ Plan is proposed in good faith
- ❑ Acceptance of the plan by all classes of creditors or at least one “impaired accepting class”
- ❑ The plan is feasible – will it actually work



# Exclusivity

- The Bankruptcy Code grants the debtor the *exclusive* right to file a plan of reorganization within the first 120 days after the petition date and the *exclusive* right to solicit votes on the plan within the first 180 days.
- The debtor may seek a one-time extension of this period, but not for more than 18 months after the petition date for filing a plan.
- After expiration of the 120 day period, any party in interest can file its own plan to reorganize or liquidate the debtor.



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# How Does This Affect You?

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A Closer Look At Executory Contracts



# A Debtor's Obligations

- A debtor has a fiduciary duty to maximize the value of the bankruptcy estate for all creditors.
- As a corollary, a debtor has authority to determine which executory contracts bring value to the estate and which do not.
  - If the executory contract is valuable to the debtor, the debtor may “assume” the contract and continue performance.
  - If the executory contract is not valuable, the debtor may “reject” the contract, or terminate it.
  - Note that a contract must be assumed or rejected in full – a debtor cannot pick and choose valuable provisions.



# Executory Contracts – Court Approval

- The decision to assume or reject an executory contract is subject to court approval.
- Court uses the “business judgment” test to evaluate a debtor’s decision.
- Debtor must have sound business judgment for assuming or rejecting a contract.



# What Happens When....

## A debtor assumes my contract?

- ❑ The debtor must cure any existing defaults.
- ❑ The debtor must continue to perform under the contract or provide “adequate assurance” that the debtor will and is able to perform.
- ❑ Often, a debtor will assume a contract, and then assign its interest to a third party for value (purchaser must provide adequate assurance).
- ❑ Bankruptcy law favors assignment – it will be allowed despite contract provisions to the contrary .



# What Happens When...

The debtor rejects my contract?

- ❑ The debtor is relieved of its obligations under the contract.
- ❑ Rejection constitutes a breach as of the day the bankruptcy case was filed.
- ❑ Rejection entitles the non-debtor party to a general unsecured claim for damages.



## Is there a deadline for a debtor to assume or reject?

- Generally, no. A debtor has until the confirmation of the plan of reorganization to decide whether to assume or reject.
- However, a non-debtor party may request that the court set an earlier deadline based on compelling circumstances.
- The court will look at:
  - The damage the non-debtor will suffer beyond the compensation available under the Bankruptcy Code
  - The importance of the contract to the debtor's business and reorganization
  - Whether the debtor had sufficient time to evaluate its financial situation and potential value of its assets
  - Whether exclusivity has been terminated
  - The complexity of the case.



# Remedies for Non-Debtor Parties to Executory Contracts

- Request that court order the debtor to decide within a specified period of time to assume or reject.
- If the debtor continues to benefit from the contract after the bankruptcy, the non-debtor party is entitled to an administrative priority claim.
- Request a relief from stay in order to terminate the contract.
- Before a debtor may assume an executory contract, it must cure all defaults or provide adequate assurance of performance.
- A general unsecured claim for defaults upon rejection.
- If it is a commodities or forward contract and the non-debtor qualifies, the contract can be terminate the contract if it provides for termination in the event of a bankruptcy (the “safe harbor provisions”).



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# Other Considerations

- A non-debtor party may not legally terminate an executory contract without obtaining the Bankruptcy Court's permission.
- A non-debtor party may negotiate with the debtor for contractual modifications.



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# VeraSun Energy Corp.



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# VeraSun Energy Corp.

- Filed Chapter 11 bankruptcy in the United States Bankruptcy Court for the District of Delaware on October 31, 2008 along with 24 subsidiaries.
- Due to lack of financing the Debtors were forced to liquidate their assets pursuant to public auction recently held on March 16, 2009.
- Valero Energy Corp. outbid ArcherDaniels Midland for the right to buy 7 – 8 plants including substantially all of the assets of
  - VeraSun Albert City, LLC and
  - ASA Albion, LLC
- AgStar Financial Services, PCA acquired:
  - US BioEnergy Corp.
  - VeraSun Central City, LLC
  - VeraSun Dyersville, LLC
  - VeraSun Hankinson, LLC
  - VeraSun Janesville, LLC
  - VeraSun Ord, LLC
  - VeraSun Woodbury, LLC
- Dougherty Funding, LLC acquired:
  - US Bio Marion, LLC
- WestLB AG acquired:
  - ASA Linden, LLC
  - ASA Bloomingburg, LLC



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# Pilgrim's Pride Corporation

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# Pilgrim's Pride Corporation

- Filed Chapter 11 bankruptcy in the United States Bankruptcy Court for the Northern District of Texas on December 1, 2008 along with 6 subsidiaries.
- Currently have a pending motion to sell chicken processing plant in Farmerville, LA for \$80 million.
- Company has is locked into many over-valued futures contracts.



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# Pacific Ethanol, Inc.

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Pacific Ethanol, Inc.

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# Pacific Ethanol, Inc.

- Recently granted a 30-day “breather” or waiver of default from hits lenders.
- Has until March 31, 2009 to generate enough cash to meet its obligations to three major lenders, or try and negotiate further forbearance agreements.
- May eventually need to file for chapter 11 bankruptcy or dilute shareholders to raise more equity.



# Questions

Please Do Not Hesitate To Contact Us With Any Questions



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