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Wanting a Seat at the Table: The Rise of Equity Committees

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I. Introduction

Over the past few years, equity holders have increasingly requested appointment of an official equity committee to represent their interests. This increased frequency of requests has been particularly noticeable in recent oil and gas cases, where equity holders have used fluctuations in commodity prices to argue for higher valuations of the debtors' assets that should generate greater returns to equity. This article examines the bases for appointment of an official equity committee and the standard that courts, particularly courts within the Fifth Circuit, have applied in evaluating such requests. This article concludes with several examples from recent cases in which equity holders requested appointment of official equity committees and evaluates whether such requests (and in some cases, the appointment of official equity committees) resulted in improved treatment of equity under the debtors' plans of reorganization.

II. Statutory Authority for Appointment of Equity Committees

The Bankruptcy Code defines an equity security holder as "a holder of an equity security of the debtor." 11 U.S.C. § 101(17). An equity security in the debtor may be (i) a share in a corporation, whether or not denominated a stock; (ii) interest of a limited partner in a limited partnership; or (iii) a warrant or a right, other than a right to convert to purchase, sell or subscribe to a share, security, or interest in a share of a corporation or interest in a limited partnership. 11 U.S.C. § 101(16).

The U.S. Trustee and bankruptcy courts have authority to appoint official committees of equity security holders in Chapter 11 cases. While it is customary to first seek appointment by the U.S. Trustee before petitioning the bankruptcy court for appointment, this step appears to only be permissive rather than required. However, given the cost of and delay that may be associated with litigating the necessity of appointment of an official equity committee, it is common for equity security holders to first seek appointment of an official equity committee through the U.S. Trustee.

The authority for appointment of an equity committee is governed by section 1102 of title 11 of the United States Code (the "Bankruptcy Code"), which provides that "as soon as practical after the order for relied under chapter 11 of this title, the United States trustee ***shall*** appoint a committee of creditors holding unsecured claims and ***may*** appoint additional committees of creditors or of equity security holders as the United States trustee ***deems appropriate***." 11 U.S.C. § 1102(a)(1) (emphasis added). Accordingly, while the U.S. Trustee is directed to appoint an official committee of unsecured creditors, appointment of an official equity committee by the U.S. Trustee is discretionary.

A party in interest may also request that the court appoint an equity committee "if necessary to ensure adequate representation . . . of equity security holders." 11 U.S.C. § 1102(a)(2). Once the court orders appointment of an equity committee, the U.S. Trustee is required to appoint the equity committee. *Id*.

The Bankruptcy Code also grants a degree of discretion to the U.S. Trustee and the court in composing an official equity committee, which "shall ordinarily consist of persons, willing to serve, that hold the seven largest amounts of equity securities of the debtor of such kind represented on the committee." 11 U.S.C. § 1102(b)(2). If not already filed in the case, the U.S. Trustee must obtain a list of the debtor's equity security holders to solicit the equity holders' interest in serving on the equity committee.

The U.S. Trustee may, but is not required to, hold a meeting of equity security holders under section 341(b) when beneficial or useful. However, the court may order, after notice and a hearing, for cause that no meeting of equity security holders be held if the debtor has filed a plan and solicited acceptances prior to the petition date. 11 U.S.C. § 341(e).

The equity committee may, with the court's approval, appoint attorneys, accountants and other agents to act on the committee's behalf. 11 U.S.C. § 1103(a). An equity committee professional may not represent any other entity with interests adverse to the equity committee, effectively limiting representation to the committee only. 11 U.S.C. § 1103(b).

III. Judicial Authority for Appointment of Equity Committees

Section 1102(a)(1) permits the appointment of a committee of equity security holders as the "United States trustee deems appropriate." In evaluating whether to appoint an equity committee, U.S. Trustees typically consider whether there is enough equity in the estate to justify the burden and expense of an equity committee. 7 COLLIER ON BANKRUPTCY ¶ 1102.03[2][a] (Alan N. Resnick & Henry J. Sommer eds., 16th ed. 2015).

In the event the U.S. Trustee declines to appoint an official equity committee upon the request of one or more equity holders, such holders can request that the bankruptcy court direct the U.S. Trustee to appoint an official equity committee. Under section 1102(a)(2) of the Bankruptcy Code, on request of a party in interest, the court may appoint a committee of equity security holders "if necessary to assure adequate representation of…equity security holders." *See also In re Village at Camp Bowie I*, 454 B.R. 702, 709-10 (Bankr. N.D. Tex. 2011).

The relevant factors for appointment of an equity committee have been described by the United States Bankruptcy Court for the Northern District of Texas as follows:

1. whether the debtors are likely to prove solvent;

2. whether equity is adequately represented by stakeholders already at the table;

3. the complexity of the debtors' cases; and

4. the likely cost to the debtors' estates of an equity committee.

In re Pilgrim's Pride Corp., 407 B.R. 211, 216 (Bankr. N.D. Tex. 2009). In *SandRidge Energy*, Judge David Jones also articulated a practical fifth factor that he considers in evaluating requests for appointment of an official equity committee—whether, given the existing constituencies in the case, the appointment of an official equity committee would add anything to the case. *See In*

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