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Recidivist Debtors: Chapter 22s of Oil and Gas Business Debtors. Why is it Happening Now?

Moderator:
Kyung S. Lee, Kyung S. Lee PLLC, Houston, TX

Panelists:
J.P. Hanson, Houlihan Lokey, New York, NY
Shari L. Heyen, Greenberg Traurig, LLP, Houston, TX
John T. Young, Jr. Conway Mackenzie, Inc., Houston TX

Written materials compiled by:
R.J. Shannon
Barron & Newburger, P.C.
Austin, TX

Frequently Asked Questions About Chapter 22 Bankruptcy Cases

By: R. J. Shannon, Barron & Newburger, P.C.

1. What is a "Chapter 22" case?

"Chapter 22" refers to repeat chapter 11 filings.[1] Although the term is used to mean any repeat chapter 11 filings by a debtor, it best describes situations when either the first chapter 11 case is still ongoing (e.g., a confirmed plan of reorganization is still being implemented) or the subsequent filing is substantially related to the same difficulties the debtor faced in the first chapter 11 case.

2. What is the prevalence of repeat filings?

From 1984-2013, approximately 15% of publicly traded companies that were acquired through or emerged from chapter 11 re-filed during that period.[2] Looking only at companies that emerged as a continuing, independent entity, the recidivism rate was approximately 18%.[3]

3. What does the Bankruptcy Code say about repeat chapter 11 filings?

The Bankruptcy Code does not prohibit repeat filings but a Chapter 22 can look like an end run around certain provisions of chapter 11. To wit, Bankruptcy Code § 1127 prohibits non-individual debtors from modifying a confirmed plan of reorganization that has been substantially consummated. The only options once the plan has been consummated are conversion to chapter 7 or dismissal under Bankruptcy Code § 1112. Further, Bankruptcy Code § 1141(a) makes the terms of a confirmed plan otherwise binding on the debtor, creditors, and equity holders. Contrary to these provisions, the practical effect of a Chapter 22 can be the amendment of the prior plan (prohibited by § 1127) and further modification of the rights between the debtor and its creditors (limiting the legal force of § 1141).

4. What have courts said about repeat chapter 11 filings?

Courts have generally analyzed repeat chapter 11 filings under a good-faith framework.[4] While a Chapter 22 can permit a debtor to improperly bypass prohibitions contained in the Bankruptcy Code, the Fifth Circuit held in *Elmwood Dev. Co. v. General Electric Pension Trust (In re*

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[1] The term "Chapter 22" was coined by Edward I. Altman and Edith S. Hotchkiss in 1993. See EDWARD I ALTMAN, CORPORATE FINANCIAL DISTRESS AND BANKRUPTCY: A COMPLETE GUIDE TO PREDICTING AND AVOIDING DISTRESS AND BANKRUPTCY 10 (2d ed. 1993); Edith S. Hotchkiss, Investment Decisions Under Chapter 11 Bankruptcy (Aug. 1993) (unpublished Ph.D. dissertation, New York University).

[2] Edward I. Altman, Revisiting the Recidivism—Chapter 22 Phenomenon in the U.S. Bankruptcy System, 8 BROOK. J. CORP. FIN. & COM. L. 253, 257 (Spring 2014).

[3] *Id.*

[4] *See, e.g.*, In re Elmwood Dev. Co., 964 F.2d 508, 511 (5th Cir. 1992); In re Jartran, Inc., 886 F.2d 859, 867 (7th Cir. 1989); In re Pulp Finish 1 Co., No. 12-13774 (SMB), In re JCP Props., 540 B.R. 596, 610 (Bankr. S.D. Tex. 2015); 2014 Bankr. LEXIS 189, at *22-23 (Bankr. S.D.N.Y. Jan. 16, 2014).

Elmwood Dev. Co.) that successive bankruptcy filings may be in good faith where unanticipated changed circumstances arise.[5]

In *In re JCP Properties*, the U.S. Bankruptcy Court for Southern District of Texas pointed out that the critical analysis conducted by the Fifth Circuit in *Elmwood* was "whether the filing of the subsequent case was so 'related in time or substance' so as to offend 'traditional notions of res judicata' and whether the debtor otherwise evidences good faith in the subsequent filing."[6] *JCP Properties* presented five factors to consider in this analysis:

(i) The length of time between the two cases;

(ii) The foreseeability and substantiality of events which ultimately caused the subsequent filing;

(iii) Whether the new plan contemplates liquidation or reorganization;

(iv) The degree to which creditors consent to the filing of the subsequent reorganization; and

(v) The extent to which an objecting creditor's rights were modified in the initial reorganization and its treatment in the subsequent case.[7]

5. How does feasibility play into this?

Bankruptcy Code § 1129(a)(11) conditions plan confirmation on a finding that "[c]onfirmation of the plan is not likely to be followed by the liquidation, or the need for further financial reorganization, of the debtor or any successor to the debtor under the plan." Courts have held that bankruptcy judges must make an independent finding of feasibility even in the absence of any objection to confirmation.[8] The goal is to prevent the need for a debtor to re-file bankruptcy.

Some commentators have called for increased judicial scrutiny of feasibility to reduce the number of Chapter 22 filings.[9] In support of this position, empirical analysis suggests that jurisdictions with laissez-faire reputations (deservingly or not) have higher rates of repeat filings than other jurisdictions.[10]

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[5] 964 F.2d at 511.

[6] 540 B.R. at 610-11.

[7] *Id.* at 611 (adopting factors from In re Bouy, Hall & Howard & Assocs., 208 B.R. 737, 744 (Bankr. S.D. Ga. 1995)).

[8] *See, e.g.*, Heartland Fed. Sav. & Loan Ass'n v. Briscoe Enters. (In re Briscoe Enters.), 994 F.2d 1160, 1166 (5th Cir. 1993); In re Charles St. African Methodist Episcopal Church of Bos., 578 B.R. 56, 94-95 (Bankr. D. Mass. 2017); In re Las Vegas Monorail Co., 462 B.R. 795, 798 (Bankr. D. Nev. 2011).

[9] *See, e.g.*, We Have a Feasibility Problem: Bankruptcy Judge Denies Confirmation in Paragon Offshore, PETITION, https://petition.substack.com/p/we-have-a-feasibility-problem.

[10] Ruth Sarah Lee, Delaware's Relevance in Chapter 22: Who Is "Courting Failure" Now?, 31 REV. BANKING & FIN. L. 443, 444-45.

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