The ‘Wall of Debt’: Identifying and Developing Long-Term Business Solutions for Near- and Medium-Term Debt Maturities

Two years into one of the worst credit crises in history, the capital markets finally are showing signs of improvement. In recent months, credit slowly has become more available at lower costs and on less restrictive terms. And the high-yield debt market arguably has stabilized, with a surge of new issuances beginning in May 2009, after having been effectively frozen the previous five quarters.

However, while there are many hopeful signs, it is too soon to conclude that the economy has recovered or that capital markets will improve. Lenders and investors continue to hoard cash, unemployment remains high, consumers remain uncertain and the federal government likely will not be an ongoing source of rescue financing in the face of soaring national debt. As a consequence, the future of the capital markets remains highly uncertain.

Moreover, one of the key challenges that will soon face Corporate America is a virtual "wall of debt" that is scheduled to mature in the near and medium term. Hundreds of billions of dollars of bank debt, high-yield debt and commercial real estate debt come due between 2010 and 2014. The staggering amount of this debt may be beyond the capacity of the leveraged-loan and high-yield markets to absorb. Even if these markets enjoy a broad recovery in the coming year, companies with deteriorating financial performance will have difficulty accessing them.

Businesses that have debt maturing within this window may face a reduced range of options, given aggregate debt maturities and the continued uncertainty plaguing the capital markets. Accordingly, leveraged businesses, their lenders and other stakeholders will need to proactively anticipate and explore business options to develop strategies for implementing value-additive business solutions long before scheduled debt maturities. Only through long-term liability management can a business maintain optionality and avoid expensive and value-destructive alternatives, such as a traditional bankruptcy filing.

There are several time-tested techniques that leveraged companies and their stakeholders can utilize in developing and implementing long-term, value-enhancing business solutions. For example, in so-called "amend-to-extend" transactions, borrowers effectively refinance their revolving credit and/or term loan facilities through loan modification amendments that allow consenting lenders to extend their maturities on a non-*pro rata* basis with the vote of a majority of the lenders. Leveraged companies also may negotiate covenant-relief amendments as well as refinancings of term loan facilities with secured and unsecured high-yield debt offerings that extend maturities and relax covenants.

A company with debt that is trading below par also may consider pursuing debt tender offers whereby it offers to purchase debt at a discount to face and a premium over its trading price. Companies also have amended their credit facilities to permit loan buybacks, on a non-*pro rata* basis, at attractive discounts. Alternatively, companies with liquidity constraints can exchange existing debt for new debt with longer maturities and other more favorable terms pursuant to debt-exchange offers structured to be exempt from the registration requirements of the securities laws, thus enabling them to be implemented quickly. Companies also can exchange existing debt for new equity securities in transactions that are exempt from the registration requirements of the securities laws.

One possible drawback of an exchange offer is that only debt holders who affirmatively agree to the proposal are bound. To mitigate against holdouts, exchange offers may be coupled with a consent

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solicitation whereby restrictive covenants in existing debt instruments are eliminated.

Another method for eliminating holdouts is to pursue a partial in-court alternative pursuant to either a "prepackaged" or "prenegotiated" Chapter 11 plan of reorganization. In this case, the Chapter 11 restructuring plan is negotiated and agreed upon by the company and a critical group of debt holders before commencement of Chapter 11 proceedings, thereby minimizing the length of the company's stay in Chapter 11. Whereas out-of-court solutions typically require 100 percent approval by affected creditors, Chapter 11 plans can be confirmed and made binding on dissenters much more easily, *i.e.*, if at least one-half of affected creditors, holding at least two-thirds in amount of affected debt, vote to accept.

Several of these techniques were employed by The CIT Group Inc. in resolving billions of dollars in debt obligations.[1] CIT pursued a cash tender offer for $1 billion of debt funded by a $3 billion rescue financing (later upsized to $7.5 billion), followed by an exchange offer with a "fall-back" prepackaged Chapter 11 reorganization plan that resulted in the elimination of approximately $10.5 billion of debt. Although this was the fifth-largest bankruptcy in history and involved $65 billion in debt, CIT was in bankruptcy for only 40 days. It is the largest and only financial institution ever to successfully file and implement a prepackaged Chapter 11 plan.

Charter Communications, Inc. successfully implemented a prenegotiated plan in a case described by the bankruptcy court as "perhaps the largest and most complex prearranged bankruptcy ever attempted, in all likelihood rank[s] among the most ambitious." Under the plan, Charter reinstated approximately $12 billion of senior secured debt, shed approximately $8 billion of debt and raised more than $1.6 billion through a fully backstopped rights offering.[2] The linchpin of the plan was a settlement with the shareholder that created more than $3 billion in tax-related value for the reorganized company.
(See "Recent Trends in Balance Sheet Restructurings Utilizing Reinstatement in Bankruptcy")

[1] Skadden represented CIT.

[2] Skadden represented the largest shareholder of Charter Communications, Inc.