

Report on Findings of Chicago Bankruptcy Focus Group Regarding Perceived Loss of Potential Chicago Corporate Chapter 11 Cases to Delaware

On July 10, 2000, Ira Bodenstein (the U.S. Trustee) and various Chicago-area bankruptcy professionals met to discuss some of the perceived reasons that so many large corporate chapter 11 cases are filed in Delaware instead of Chicago. The meeting was held under the auspices of a subcommittee of the Chicago Bar Association Bankruptcy and Reorganization Committee chaired by Neville Reid. Below is a list of the main issues and concerns which members addressed at the meeting (and the views of professionals not in attendance but who were consulted after the meeting) and which the group would like to discuss with the Chicago bankruptcy judges at the earliest opportunity:

1. **General Reasons for Delaware Filings**: In general, larger companies which could legally file a complex chapter 11 case in Chicago tend to file those cases in Delaware (often upon the recommendation of their counsel, consultants key creditors and equity holders) for a number of reasons, some of which are listed below (not necessarily in order of priority):

a. **Perceived Predictability and Certainty**: Delaware judges are generally perceived as being more predictable as to how they will rule on certain key issues affecting the debtor's reorganization. Delaware judges are perceived as having developed an informal 'consensus' view on material issues such as DIP financing, cash collateral, exclusivity and conflicts of interest. Judge Walsh, for example, has from time to time issued letters and guidelines describing the kinds of provisions he will generally approve (or disapprove) in proposed cash collateral orders. Chicago judges are perceived as not having developed any such consensus on these issues, and the resulting perceived uncertainty deters filings in Chicago.

b. **Perceived Experience Gap**: Delaware judges are generally perceived as having more experience in large, complex chapter 11 cases relative to judges in Chicago or other parts of the country. This gives both debtors and their main creditor constituencies confidence that the case will be well-managed by the court, and that rulings on significant and complicated threshold issues will be made promptly in the case.

c. **Perceived Deference to Debtor and Affected Constituencies**: Delaware judges are generally perceived as being more deferential to agreements reached between the debtor and those key creditor constituencies whose economic interests are chiefly affected by the issues covered by the agreement. Chicago judges are generally perceived as being less deferential and more circumspect of such agreements. Thus, creditors (e.g., DIP lenders) who reach agreements with debtors on key business issues in the case will themselves often favor a Delaware filing to avoid the adverse risk that the agreement may unravel.

d. Perceived Body of Case Law: It is perceived that Delaware has a well defined body of case law on various issues, which arise in a chapter 11 case. This eliminates uncertainty which could arise if the case were filed in Chicago.

e. Perceived Relative Ease of First Day Motions: Delaware judges are perceived as moving first day motions along more quickly, and with greater deference to the debtor's business judgment and the interests of key vendors necessary to sustain the business, relative to Chicago judges. Several bankruptcy professionals have commented that potential DIP lenders, whose loans are essential to sustaining the business, actually prefer that the debtor file in Delaware and not in Chicago because of their confidence that an order is likely to be entered on the first day in Delaware without much difficulty. There is also the perception that payment of pre-petition unsecured debt under the necessity doctrine is more acceptable in Delaware than in Chicago or elsewhere, further facilitating first day relief. Members also noted, however, that there is a legitimate debate among judges outside of Delaware as to the extent and legality of first day relief insofar as it involves the payment of pre-petition debt.

A close corollary of the general efficiency of first day hearings in Delaware cases is that the Delaware judges' procedures for administering complex chapter 11 cases reduce uncertainty and tend to discourage precipitous litigation. For example, each Delaware case is usually set for a biweekly or monthly status hearing, at which time numerous motions are heard and ruled on. This approach tends to provide procedural certainty and structure to the case and encourage parties to negotiate and resolve differences between status calls, without the need for intervening litigation. By contrast, the "2-day notice" rule in Chicago is perceived as encouraging some parties to harass or burden the debtor with frequent, litigious motions. The 2-day rule can leave the debtor's counsel with inadequate time to prepare. It should be noted, however, that many professionals like the 2-day rule for other reasons, including that relief on routine matters (e.g., professional retention applications and discovery motions) can be addressed on a shorter time frame than might otherwise be the case in Delaware or other courts.

f. Conflict of Interest Issues for Professionals: Some professionals have expressed concern that conflict of interest issues regarding retention applications seem more easily resolved in Delaware than in Chicago, typically by simply greater disclosure. Other professionals have indicated that it is generally no less difficult to get retained in Chicago than in Delaware, although many more parties seem to object to fee applications in Chicago than in Delaware. This may be a function of greater perceived

collegiality among professionals in Delaware are than in Chicago.^{1/} Additionally, some practitioners commented that in Delaware, out of town lawyers are paid their customary rates, while this issue is perceived as unclear in Chicago.

In general, all of the above has provided greater 'business certainty' for filing in Delaware. Bankruptcy professionals advising clients on where to file their cases generally consider Delaware a 'safe choice' and are reluctant to run the risk of filing outside of Delaware and not have the case be administered as smoothly as it would likely have been administered in Delaware. For most professionals, the competition for potential clients is far too competitive to incur that kind of a risk.

At the same time, Chicago bankruptcy professionals have also recognized that they have some responsibility to encourage their clients to file more cases in Chicago so that a more favorable perception of the Chicago bankruptcy system can take hold. Also, professionals have urged greater cooperation and dialogue between the Chicago bankruptcy bar and the Chicago area judges on the Delaware issue, the underlying causes behind it, and other matters that may arise.

2. Some Questions for a Session with the Judges:

- a. While perception has a tendency to become reality, the foregoing perceptions may not seem fair. Do the Chicago judges believe that any of the reasons expressed above are fair? What is their view as to why corporate debtors appear to bypass Chicago and file in Delaware?
- b. Should the Local Bankruptcy Rules be amended to facilitate the administration of complex chapter 11 cases, including rules which (i) expedite hearings on first day orders and provide guidelines as to the form for, and criteria for approval of, first day motions, (ii) establish special biweekly or monthly status calls for complex chapter 11 cases, and (iii) provide criteria for acceptable provisions in motions and proposed orders regarding cash collateral, DIP financing, the payment of pre-petition indebtedness and other issues generally applicable to complex chapter 11 cases?
- c. What measures or steps can be taken to improve the dialogue between Chicago judges and the Chicago bankruptcy bar?
- d. Would the judges consider reaching a consensus on issues germane to complex chapter 11 cases, such as DIP financing and requests for

^{1/}Some professionals have commented that despite the greater general collegiality in Delaware, fee applications are currently backlogged in Delaware due to the heavy caseload. This fact alone could result in more cases being filed outside of Delaware, or being transferred out of Delaware back to Chicago and other jurisdictions on disputes over venue.

the extension of the exclusivity period? Would the judges be willing to publish that consensus?