The Distressed Debt Report

News, Information, and Analysis of Distressed Debt in the Middle Market

Volume V, No. 10 distresseddebt.dealflowmedia.com May 26, 2009

IN THIS ISSUE

EUROPEAN INSOLVENCY LAW STRUGGLES TO GET AHEAD OF SOARING DEFAULTS

by Reg Crowder

Despite the challenge of coping with Europe's many distinct and rapidly-changing insolvency laws, there is serious money to be made restructuring European companies as the lingering global recession drags more of them into insolvency.

That was a point made repeatedly by European turnaround experts speaking at a webinar on the reform of European insolvency laws sponsored by the Turnaround Management Association.

"There is money to be made if you do it the right way," said Alain Le Berre, managing director in the London office of **Huron Consulting Group**, which helps international clients complete restructurings across multiple national jurisdictions.

Even in France where the insolvency laws strongly emphasize the preservation of jobs, companies in trouble can be restructured to become profitable again, he said.

"If you think it is impossible to close plants and lay off employees in France or in Germany then you are mistaken," Le Berre said. "Nothing is less true than this. But there is an operating manual. If you know how to do it properly, you can get it done."

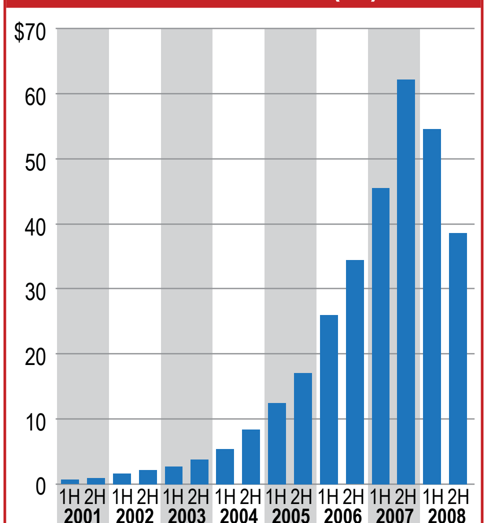
On the other hand, people who come to any of the European countries and attempt "DIY" (do-it-yourself) restructuring deals without getting local legal and accounting advice regularly run into a lot of problems, he said.

The comments come as the rate of business insolvencies in Europe is expected to soar in the next two years to its highest rate in modern history.

Standard & Poor's projects that by the end of 2010 the cumulative default rate will exceed 20% among bond-issuing companies whose credit is rated as "speculative" by S&P. Based upon that projection, between 60 and 75 European companies with speculative-rated debt will default in 2009 and about the same number will default on their debt in 2010, the credit rating agency said.

Continued on page 11

NOTIONAL VALUE OF CDS CONTRACTS ($T)



Source: International Swaps and Derivatives Association

LEHMAN CASE MAY SHOW CDS EFFECT ON BANKRUPTCIES

Conflicts of Interest Possible Among Holders of Swaps

by Terence Flanagan

Prior to the emergence of credit default swaps (CDS), other derivatives, and securitization, bankruptcy cases were largely straightforward and transparent, at least as far as the motives of involved parties. The legal system assumed the package of rights that typically comes with ownership of debt – economic rights, contractual control rights, and other legal rights – were bundled together, and that creditors wanted to keep solvent companies out of bankruptcy and to maximize the value of insolvent firms.

Advances in financial engineering have rendered those assumptions no longer fully reliable. CDS have been especially nettlesome in this regard, as the notional value of the derivatives has grown to a multiple of the underly-

Continued on page 9

The Distressed Debt Report

DealFlow Media, Inc.
P.O. Box 122
Syosset, NY 11791
T (516) 876-8006
F (516) 876-8010

subscribe@dealflowmedia.com
www.dealflowmedia.com

The Distressed Debt Report™ is published on the second and fourth Tuesday of every month, except the second Tuesday of August and the fourth Tuesday of December. Subscription rate: $1,595 per year for 22 issues, delivered electronically.

DON'T DO IT, LEHMAN BROTHERS!

Depressed Prices Mean Spin-off May Not Be Worth It

by Liz Enochs

A **Lehman Brothers** spin-off couldn't come at a worse time. That's what market participants and observers say in response to recent reports suggesting that the bankrupt investment bank is considering selling off a portion of its remaining assets to investors looking for deals on distressed properties.

Lehman is taking steps to spin off its remaining real estate and private equity holdings into a company insiders are tentatively calling Lamco, for Legacy Asset Management Co., according to a May 14 article in the *Wall Street Journal*. While Lehman expects the assets to garner about $45 billion in the current market, the firm valued the portfolio, which includes consumer mortgages, corporate bank debt and Miami condos, at around $400 billion at nondistressed prices, the *Journal* reported.

Selling those assets now could be a big mistake, said Chuck Carlson, a portfolio manager at **Horizon Investment Services** in Hammond, Ind. "Any time you have that kind of supply coming into a marketplace, potentially, it's just one more amount of supply that's probably going to depress prices," he said. "If I was sitting with comparable stuff, I'm not sure I'd be real thrilled to see that kind of supply come into the market and establish a real price floor, and then in turn I've got to mark to market."

Benjamin Bornstein, a managing partner with **Indigo Asset Management** in Scarsdale, N.Y., agreed. "If you want to go and force these things for sale now, you're just going to get horrendous pricing — there's no doubt about that," he said. "The problem is that the size of Lehman is just so huge."

With a portfolio worth $400 billion at its peak, observers suggested that any attempt to put all those assets on the market at once could tilt the playing field and depress prices for all market participants.

However, those managing the Lehman bankruptcy may be looking at running the spun-off company themselves rather than selling it to buyers of distressed assets, said two former Lehman employees now working at a private equity firm.

Especially when considering private-equity investments into which Lehman has already put more than 50% of the capital it committed, "it's economically in the best interest of the creditors to continue funding the investment to fruition and try to get the value out," said one of the former employees. "To sell in the secondary market right now, whatever the discounts might be, would be to get a lower number for people in the bankruptcy."

And those discounts are reportedly steep. According to a partner in one private equity firm, "most private equity assets are trading at 50%-plus discounts to their December net asset values, so it's a fairly deep haircut."

Lehman may be selling off some of its private equity interests that are not heavily funded, but it's likely retaining its more highly funded assets in the pool of assets known as Lamco, according to the former employees. "Since they're more mature, that means the underlying companies are more mature and closer to liquidity," said one of the former employees.

"There's actually enough cash on the balance sheet that has been set aside in this larger bankruptcy process for them to fund this process" of fully paying into funds in which Lehman is already heavily invested, he added. Plus, it's possible the real estate assets in the Lamco pool could help keep the cash flowing, he added.

Another alternative to a spin-off would be to put the Lehman assets into a liquidating trust that could collect the assets and resolve the liabilities over a long period of time, said Bornstein of Indigo Asset Management. However, "people are probably not going to be happy taking back pieces of paper in a long-term liquidating trust," he said. "But the alternative to that is just a terrible, terrible fire sale."

At non-distressed prices, "there's just nobody that's got that kind of capital to write a check, except maybe the Sultan of Brunei," said Bornstein. "Even at 10 cents on the dollar, who can write $40 billion checks?"

The news regarding a potential Lehman spinoff isn't all bad, though, said at least one observer. Michael Molinaro, a partner with **Loeb & Loeb**, a Chicago law firm that handles a large number of bankruptcy cases, said his clients' behavior — reflecting a "renewed interest in activity" — has begun to suggest that at least some think the market for distressed assets has hit the bottom.

Although his clients are still being selective about investing, "Where they think there's a strategic fit, they're now inclined to investigate, do due diligence and see if they're going to pull the trigger, whereas they were not inclined to do that a couple of months ago," he said.

Meanwhile, until that investor interest gets reflected in deal pricing, "the vultures are probably going to be pretty excited" about a possible Lehman Brothers spinoff, said Carlson.

Thrift Regulators Considering More PE Deals

Private equity firms apparently are turning their attention to thrifts as the Federal Reserve has restricted PE firms from acquiring control of banks.

The Office of Thrift Supervision has seen an increasing number of inquiries from private investors ever since the agency approved the sale of **Flagstar Bancorp** of Troy, Mich., in January, according to William Ruberry, an agency spokesman. The OTS continues to entertain similar deals, he said.

"We received a lot of inquires," Ruberry said in an interview. "We are continuing to talk with private equity parties about what they might do."

The OTS declined to say how many deals were being reviewed or reveal the names of any companies involved. The OTS is at odds with the Federal Reserve which has told private equity companies that it won't allow entities that aren't regulated as banks to own majority stakes in lenders, *Bloomberg News* has reported. The differing regulatory approaches may encourage more private equity deals for thrifts.

Laws governing the acquisition of thrifts, which are regulated by the OTS, and bank holding companies, which are regulated by the Federal Reserve, are different, according to Patricia McCoy, professor at the University of Connecticut School of Law.

"As a matter of historical accident they turned out differently," she told *The Distressed Debt Report*. The authorizing statute regarding thrifts is more "flexible" than the one for banks, she said. "The Fed is simply saying we are not going to let a private equity firm get control of a bank."

The Federal Reserve expects the parents of bank holding companies to provide capital if needed to financial institutions. The structure of private equity funds makes it unlikely that they would be willing to provide such funding, she said.

Officials at the OTS are not developing a comprehensive standard for approving these deals since each are very different, Ruberry said.

Like banking regulators, the OTS is concerned about undercapitalized thrifts that may be in danger of becoming insolvent. McCoy said that the OTS also is fighting for its survival as the number of financial institutions it regulates has been dwindling over the past few years.

"The Sword of Damocles has been over the agency for the past decade," she said. "Virtually its entire operating budget comes from fees."

Bank regulators' opposition to PE firms buying banks stems from regulations designed to protect a financial institution's assets from being siphoned off by outside investors.

Investors, including billionaire Wilbur Ross, have complained about the restrictions. Ross and his fellow billionaire J. Christopher Flowers acquired banks using their personal money. Many other private equity players are remaining on the sidelines until the rules are sorted out, analysts said.

Blackstone Group and **Carlyle Group**, the two largest leveraged buyout firms, are among the players eager to snap-up distressed banks whose valuations have plunged because of the economic crisis, according to *Bloomberg*. Neither company would comment to *The Distressed Debt Report*.

Private equity companies are attracted to thrifts and other small community banks because many were conservatively managed and avoided making risky bets in markets such as mortgage-backed securities which wreaked havoc on larger financial institutions.

"These small community banks have fared pretty well," said Anthony McSwieney, senior vice president and analyst at credit rating agency A.M. Best Co., in an interview. "A lot of them are better off than the media is painting them. There is more of a motivation for private equity to get into these institutions than for these institutions to have them."

TALF Extended to Old CMBS Loans

After months of speculation, the Federal Reserve announced last week that it would include commercial mortgage-backed securities (CMBS) issued before Jan. 1 of this year in the $1 trillion Term Asset-Backed Securities Loan Facility (TALF).

Known as "legacy CMBS," the assets will be eligible for TALF financing in late July.

The announcement followed the Fed's decision in early May to extend TALF only to new CMBS transactions. However, it later added older CMBS assets after a "muted and negative market reaction" greeted the initial plan, said the Commercial Mortgage Securities Association.

CMSA has lobbied for the inclusion of new and legacy CMBS in the TALF for the last several months. Some $150 billion in securitized commercial property loans are set to mature over the next three years. No CMBS issuances have occurred in the U.S. since the market shut down after the second quarter last year, and commercial property owners with healthy assets but maturing debt for months have faced the prospect of defaulting on their loans.

Although it continues to work out terms and conditions for the program, the Fed said that both new and legacy CMBS must have at least two triple-A ratings from Fitch Ratings, Standard & Poor's, Moody's, DBRS and Realpoint.

The Fed also said it would reject any CMBS bonds that fail to meet its terms or pose an unacceptable risk. Factors that the Fed will consider in deciding whether to accept legacy CMBS will include a loan pool's cumulative losses and delinquent loans as well as how highly the pool is concentrated on certain borrowers, property types and regions.

Liquidator Goes Public in $305M Deal

Great American Group, an adviser to companies in liquidation, is going public through a business combination with blank check company **Alternative Asset Management Acquisition Corp.**

Since 1995, Great American has participated in liquidations and auctions of assets totaling about $30 billion. Its clients have included **Mervyns**, **Whitehall Jewelers**, **Circuit City** and **Tower Records**. Great American is based in Woodland Hills, Calif.

Andrew Gumaer, Great American's CEO, said in a statement that the transaction will "provide us with capital to fuel future growth initiatives and will further incentivize our team members and enhance our recruiting efforts."

In the deal valued at $305 million, Great American members will receive $120 million in cash and shares of Alternative Asset stock. Great American shareholders can also earn an additional $25 million in cash and 10 million additional shares if the company reaches EBITDA milestones.

Alternative Asset is a "SPAC" or special purpose acquisition company. A company structured as a SPAC goes public with a management team experienced in a particular sector, but the company does not initially have an actual business operation. Instead, IPO funds are escrowed while management seeks an acquisition candidate that wants to go public. If an acquisition is not consummated within 18 months, the SPAC is usually liquidated.

IPayment CEO Files for Personal Bankruptcy after $300M Legal Judgment

Greg Daily, the chief executive of credit-card processor **iPayment Inc.**, is facing a $300 million legal judgment for blocking an investment in the company. Daily filed for Chapter 11 bankruptcy protection on May 11.

The fight that led to Daily seeking protection from creditors dates to 2000. A California state jury found earlier this month that the executive interfered with two contracts between **Auerbach Acquisition Associates** and a predecessor firm of iPayment's known as **Creditcards.com**. These contracts allowed Auerbach the option to purchase a 57% ownership interest in exchange for an investment of $26 million, according to *Ecommerce*

Journal. In 2000, Auerbach tried to exercise its option but was not permitted to close the transaction.

After the California state court found that Daily had interfered with the transaction, iPayment issued a press release pointing out that the legal action was against Daily personally and not the company.

Exactly what this will mean for Nashville, Tenn.-based iPayment remains to be seen. It seems unlikely that Daily will be able to afford such a large legal judgment. Bankruptcy filings show that he had a monthly income of $14,580.11. Besides owing money to Auerbach, Daily also in hock to his lawyers for millions of dollars.

The CEO's legal woes could not have come at a worse time for iPayment. In the three months ended March 31, the company posted a net loss of $210,000, compared with net income of $1.33 million in the year-earlier quarter. IPayment is a provider of credit and debit card-based payment processing services to approximately 145,000 small merchants across the U.S.

As of Dec. 31, iPayment had consolidated debt of $687.3 million, $494.6 million of which was senior indebtedness. In financial filings, the company has described its level of indebtedness as substantial.

Former Fuel Company CEO Claims He Was Swindled in Merger

The former CEO of bankrupt **Crescent Fuels** filed a lawsuit accusing investor Frank Crivello and associates of swindling the company in an aborted merger last year that led to Crescent's restructuring and left the CEO personally liable for millions of dollars in debt.

Crescent Fuels filed for Chapter 11 protection in the U.S. Bankruptcy Court for Kansas in February. Former CEO Phillip Near filed a suit against Crivello and others involved in the merger on May 7 in the U.S. District Court for Kansas.

The suit says that Crivello proposed a merger plan involving a business combination with **Titan Global Holdings**. The plan was really a scam to steal Crescent's assets, Near claims.

Titan is the defendant in 19 ongoing collections and performance lawsuits, according to a recent filing with the Securities and Exchange Commission.

Crescent was an Independence, Kan.-based fuel seller. When Crivello approached the company in mid-2008, it was distributing 300 million gallons of fuel yearly through 340 gas stations and other outlets.

Near provided personal guarantees on most Crescent debt, including a $38 million note and line of credit from **Marshall & Isley Bank**.

Crescent was seeking a merger partner or equity investor to help finance its expansion. Last year, Near met with principals of Titan and its subsidiary Appalachian Oil Co., also known as Appco.

Titan Chairman David Marks, CEO Bryan Chance and Crivello, an investor in Titan, told Near that Titan acquired energy companies to assist in their expansion and provide them with a platform for marketing renewable fuels such as ethanol, according to the lawsuit. Near alleges that Crivello told him on several occasions that renewable fuel was "the next dot.com."

The three suggested that Titan's acquisition of Crescent through a merger with Appco would create a potent "synergy" for all three companies. Near's lawsuit claims that Crivello proposed an acquisition whose consideration would include buying out the Marshall & Isley Bank debt guaranteed by Near.

Near alleges that Crivello, Marks and Chance fraudulently claimed an impressive record of successes in the energy sector, while in reality they had met with little success. Crivello also allegedly concealed a criminal conviction, involvement in other financial lawsuits, and a personal bankruptcy. (In 1992, Crivello fraudulently used a construction loan to pay legal fees, according to Wisconsin state court records.)

Near alleges that Crivello made false assertions that **Greystone Business Credit** would purchase the debt that Near had guaranteed. Crivello then allegedly failed to live up to an October acquisition agreement that required Crescent to exchange its equity interest for stock in Titan, a nominal cash payment, and elimination of debt owed to Marshall & Isley Bank.

Crivello took delivery of Crescent shares and escrowed them with Chicago-based law firm **Goldberg Krohn**, according to the suit. The law firm allegedly returned certificates for Crescent subsidiaries but refused to return the certificate for the parent company.

Near alleges that Crivello proposed another transaction in December of last year, but the transaction fell through, leaving Near on the hook for over $40 million in debt and Crivello's associates in control of Crescent.

In January, Marshall & Isley Bank declared a default on the $38.3 million loan guaranteed by Near and froze Crescent's bank accounts. Crescent sought bankruptcy protection a week later.

Near alleges that the uncompleted merger left him responsible for additional debts including $5 million owed to fuel vendors, $6 million in fuel taxes, and $1 million for lease guarantees.

Crivello, Marks, and Chance also enriched themselves illegally through the acquisition of Appco in 2007, according to the complaint, which alleges the three ran the company into the ground after awarding Crivello a $750,000 finder's fee and diverting half the company's daily receipts to a lockbox owned by Greystone.

Crivello Group was also the object of fraud allegations in the bankruptcy of New Jersey nightclub operator **Headliners Entertainment**. In December, a bankruptcy trustee filed a fraudulent transfer suit against asset-backed lender **Yorkville Advisors** (then known as **Cornell Capital**).

Although the suit did not name Crivello as a defendant, the trustee alleged that Crivello Group principal Frank Orlando engaged in undisclosed negotiations to acquire Headliners after he was installed as its chief restructuring officer. The suit also alleges that either Yorkville or Orlando hid or destroyed Headliners' financial records.

Representatives of Yorkville, which invested in three Titan Global private placement equity financings in 2006 and 2007, declined to comment on the Headliners and Crescent Fuel suits.

The defendants in the Crescent Fuels suit have not filed an answer yet.

Calls to Crivello, Goldberg Kohn, and Greystone were not returned.

Near's attorney, Michael Pospisil of the Kansas City, Mo.-based **Edgar Law Firm**, said that he has been unable to locate Crivello to serve him with the complaint.

Yellowstone Auction Leaves Fraud Claims on Block

The contentious bankruptcy proceedings of Montana's **Yellowstone Mountain Club** moved forward when the resort was auctioned off to **CrossHarbor Capital Partners** on May 18. CrossHarbor agreed to pay $35 million in cash and an $80 million note.

But the sale did not put an end to litigation involving claims that Yellowstone principals enriched themselves illegally with hundreds of millions of dollars from $375 million in loans provided by **Credit Suisse** in 2005.

Suits alleging misappropriation have been filed by parties including the unsecured creditors committee and members of the exclusive Yellowstone Mountain Club resort. The suits' claims are not affected by the auction, said J. Thomas Beckett, an attorney with the law firm of **Parsons Behle & Latimer** who represents the unsecured creditors committee.

Owners of the Yellowstone Mountain Club lined their own pockets with over $300 million borrowed from Credit Suisse, according to the lawsuits.

A trial in the creditor suit was postponed last month, when a federal judge gave defendants extra time to review discovery documents.

The suits allege that proceeds from the loans were fraudulently diverted by principals Tim and Edra Blixseth to individual accounts and holding company **BGI**. The Blixseths later divorced, leaving Edra Blixseth as the sole owner of the resort. By that time, proceeds from the loans had allegedly been used for purposes including the purchase of properties such as the Tamarindo Resort on Mexico's Pacific coast and the 12th century Chateau de Farcheville near Paris.

An attorney familiar with the case said that recovery efforts may be focused on Tim Blixseth. "The plan will create a litigation trust, the proceeds of which will go to unsecured creditors and the Credit Suisse group," the attorney said in an email. "I understand that suing Tim will be a focus of that trust. I presume that trying to collect from BGI (which Edra now owns, post divorce) will also be a goal."

Edra Blixseth sought bankruptcy protection in March. On May 15, the bankruptcy judge signed an order authorizing Yellowstone debtors to take "any and all actions" to sell Chateau de Farcheville, which was originally purchased for $28 million, according to *Fortune Magazine*.

Heller Faces $50M Suit from Patent Client, Inter-Creditor Dispute

Bankrupt law firm **Heller Ehrman** is facing a lawsuit from a prominent former client of its patent law practice, who now seeks $50 million in damages.

At the same time, Heller's lenders and unsecured creditors are embroiled in a dispute over another $50 million.

Heller filed for Chapter 11 bankruptcy protection in December in the U.S. Bankruptcy Court for the Northern District of California. Founded in 1890, the San Francisco-based law firm had 13 offices around the world and more than 700 lawyers before it dissolved.

Former patent law client **Ron A. Katz Technology Licensing** filed a lawsuit last month against Heller for $50 million, accusing the firm of failing to pursue patent suits.

Katz and his patent holding company have sued numerous firms over their use of telephony dependent on patents he claims to own. Katz has been so assiduous in litigating that in 2005, *Forbes* magazine referred to him as a "telecom patent king" who was seeking $2 billion in fees by 2009 on 52 patents.

Katz's lawsuit against Heller states that the patent company is owed costs for which it paid the law firm in advance.

Attorneys who were working on suits for Katz were among 14 intellectual property lawyers who left Heller in September. Katz claims in the suit against Heller that conflict-of-interest issues made it impossible for some of those attorneys to continue working on the cases after the attorneys went to other firms.

The flight of the 14 partners and the loss of their billings were important factors in Heller's decision to dissolve, according to reports in the media.

A response to the patent suit has not been filed.

Meanwhile, Heller's unsecured creditors are suing lenders to avoid more than $50 million in transfers to repay loans that the banks claim were secured obligations.

Partners voted to dissolve Heller in September, after a dearth of litigation had cut revenues, partners had left the firm, and attempts to merge with other law firms failed.

The exodus of partners triggered defaults on loans from agent **Bank of America** and from **Citibank**, according to Heller's court filings.

Heller paid out more than $7 million to 35 departing or retiring partners in 2008. During the 90 days prior to the bankruptcy filing date, it also repaid Bank of America $51.4 million, followed by another $6.46 million after the petition was filed.

Then, a few weeks after Heller's dissolution, Bank of America filed a Uniform Commercial Code form seeking to correct what it called a clerical error in a 2007 filing that terminated the bank's security interest in the loans to Heller.

In March, the unsecured creditors committee asked the court to allow it to file an adversary proceeding seeking the return of $57.9 million that had been transferred to the bank in the months before and after the bankruptcy filing. The creditors argued that the bank had failed to perfect its security interest.

The bank argued that the clerical error did not invalidate its security interest. But in April the judge allowed creditors to sue.

The bank has yet to file its reply.

Tang Drops Cell Genesys Suit for Debt Exchange

Hedge fund **Tang Capital Partners** dropped a lawsuit against **Cell Genesys** after the moribund oncology treatment developer agreed to a $68 million debt swap.

Last September, Cell Genesys announced clinical trial results indicating that patients taking its Taxotere prostate cancer medication died more frequently that those in a control group. The South San Francisco, Calif.-based company has since fired 95% of its staff. It has no ongoing operations.

On May 5, San Diego-based Tang Capital filed a lawsuit against Cell Genesys demanding a declaration that the company is insolvent and prohibiting it from making executive retention payments of $2.7 million. The suit was filed in Delaware's Court of the Chancery.

On May 11, Cell Genesys said that Tang agreed to drop the lawsuit in exchange for a settlement that would include the exchange of Tang's $46.2 million in Cell Genesys 3.125% convertible senior notes due 2011 for cash, stock and new debt.

Tang owns about 73% of the note issue that totals $63.2 million in principal outstanding. The agreement to drop the suit is conditional on participation in the debt exchange by holders of 87.5% of the notes. Other buyers who purchased notes in the $145 million private placement in 2004 include **BNP Paribas**, **Argent Financial Group**, and **DKR Management**.

For each $1,000 of notes held, noteholders would receive $500 in cash plus accrued interest, $140 worth of common stock and $310 in new notes due 2013.

NHL, Phoenix Coyotes Owner Ordered to Mediation

A bankruptcy judge ordered the National Hockey League and Phoenix Coyotes owner Jerry Moyes on May 19 to mediate their dispute over a possible change of location for the Coyotes hockey franchise. The city of Glendale, Ariz., filed a suit on the same day to keep the team in Glendale.

Moyes filed a petition for Chapter 11 protection on May 5 in the U.S. Bankruptcy Court for Arizona. Moyes is the largest unsecured creditor, and the organization owes him $103.8 million.

Jim Balsillie, co-CEO of Blackberry maker **Research in Motion**, has extended a $212 million offer to buy the financially strapped Coyotes. Balsillie's offer is contingent on moving the franchise to Ontario, Canada.

NHL Commissioner Gary Bettman said in May 18 court filings that he and the NHL assumed control of the Coyotes after the NHL loaned money to the team in November. Bettman also distinguished between ownership of the team and the right to operate a franchise in Arizona. The right does not extend to operating the franchise in another location, the NHL argues.

The city of Glendale's lawsuit argues that the team's departure would cause financial damage and loss of jobs that could not be mitigated by a damages award.

In the event of a change in venue for the team, the Chapter 11 proceeding could let the Coyotes dodge a $750 million penalty for breaking the team's 30-year lease with Jobing.com Arena.

The following tables include data about publicly traded companies that have filed for bankruptcy and that have defaulted on debt in the 30 days through May 21. Data is provided by Capital IQ.

Public Company Bankruptcies

Company (Ticker)	Date	Enterprise Value (M)	Market Cap (M)	Revenue (M)	EBITDA (M)	Net Income (M)	Total Debt (M)
ION Media Networks (OTCPK:IION)	May 19	-	-	-	-	-	-
TXCO Resources (NasdaqGM:TXCO)	May 17	222.7	13.5	141.7	85.9	5.88	154.5
ICO Global Communications (NasdaqGM:ICOG)	May 15	896.9	133.2	-	-59.0	-118.6	761.1
RR Valve, Inc.	May 14	-	-	-	-	-	-
Nanogen Inc. (OTCPK:NGEN)	May 13	25.2	4.21	46.9	-18.0	-38.1	24.1
Energytec Inc. (OTCPK:EYTC)	May 13	-	0.24	-	-	-	-
RR Valve Inc.	May 13	-	-	-	-	-	-
NCT Group Inc. (OTCPK:NCTI)	May 12	-	0.09	-	-	-	-
Capital Corp. of the West (OTCPK:CCOW.Q)	May 11	-	0.32	39.3	-	78.5	275.6
Hayes Lemmerz International (NasdaqGM:HAYZ)	May 11	632.8	4.42	1,904.3	148.4	-371.7	670.1
Soyo Group (OTCBB:SOYO.E)	May 5	26.2	0.55	125.1	4.76	0.46	27.8
Filene's Basement (OTCPK:BSMT.Q)	May 4	-	-	-	-	-	-
Geely Automobile Holdings (SEHK:175)	May 4	1,462.4	1,155.3	628.5	39.7	128.8	424.3
Energy Partners Ltd. (OTCPK:ERPL.Q)	May 1	442.1	3.24	431.9	260.2	-32.7	484.5
Thornburg Mortgage (OTCPK:THMR.Q)	May 1	-	6.27	-1,702.5	-	-3,360.0	34,191.9
Industrial Enterprises of America (OTCPK:IEAM)	Apr 30	-	0.18	-	-	-	-
US Shipping Partners OTCPK:USSP.Q)	Apr 29	627.3	1.64	193.4	29.5	-97.3	460.0
American Community Newspapers (OTCPK:ACNI.Q)	Apr 28	147.1	0.44	67.0	11.9	-120.7	140.0
Source Interlink Cos. (OTCPK:SORC.Q)	Apr 28	1,413.3	3.19	2,488.3	171.3	-360.8	1,377.8
Medcom USA (OTCBB:EMED.Q)	Apr 21	8.29	3.08	2.36	0.47	0.96	5.94

Debt Defaults

Company (Ticker)	Date	Revenue (M)	EBITDA (M)	Total Debt (M)
Consolidated Beacon Resources (TSXV:KBC)	May 13	-	-0.42	0.58
Baseline Oil & Gas (OTCBB:BOGA)	May 12	37.4	15.6	123.7
ISCO International (OTCBB:ISOO.E)	May 5	10.4	-7.15	15.9
Tetragenex Pharmaceuticals (OTCBB:TTRX)	Apr 28	-	-1.24	2.19
China Cablecom Holdings Ltd. (NasdaqCM:CABL)	Apr 27	23.4	-	133.4
Comstock Homebuilding Cos. (NasdaqGM:CHCI)	Apr 24	46.7	-6.27	102.8
Firstgold Corp. (OTCBB:FGOC)	Apr 23	1.27	-10.3	0.86
TXCO Resources (NasdaqGM:TXCO)	Apr 22	141.7	85.9	154.5

Continued from front page

ing debt market. Indeed, from 2000 to 2008, the CDS market ballooned from $900 million to more than $45.5 trillion.

Credit default swaps can muddle the traditional relationship between creditor and debtor. A creditor who hedges a bond position with a credit default swap retains full contractual rights under the bond indenture, and full voting rights in bankruptcy. However, the CDS position may be greater than the cash bond position, in which case the creditor has negative economic ownership and incentive to act against the interests of the company and of other creditors of the same class.

Disclosure of firms' CDS hedging positions is scant at best, so it's rarely known when an investor has negative economic ownership of a company's debt or how common the situation has become.

The threat that CDS pose to the traditional bankruptcy dynamic was brought to light in early 2008 by researchers Henry Hu and Bernard Black of the University of Texas. But at the time, the economic turmoil in the U.S. was at an early stage and bankruptcy cases in the CDS era were few, so the impact of CDS was largely a matter of speculation. Since then, the number of corporate bankruptcies rose by 54% in 2008 compared with 2007, and prominent names such as **Lehman Brothers**, **Washington Mutual**, **Nortel Networks** and **Chrysler** have filed for bankruptcy.

Lehman Benchmark

Practitioners point to Lehman as the benchmark among CDS-touched bankruptcy cases. "Lehman Brothers has been the most notable case to date," said John Lovi, a partner in the corporate, securities and finance practice of law firm **Steptoe & Johnson** in New York. "It will also be the case to watch going forward. We may see new law forged from just this case."

Lehman filed for bankruptcy in September, triggering contractual payouts on hundreds of billions of dollars of CDS contracts that were held by hedge funds and other investment firms that had speculated on whether Lehman would survive. An October settlement set the recovery rate for Lehman's senior debt at 8.625 cents on the dollar, leaving sellers of Lehman CDS on the hook for the remaining 91.375 cents.

Separately, Lehman itself was a trading counterparty to billions of dollars worth of CDS written on other credits. These claims will be settled over the course of the bankruptcy.

However, the existence of CDS did not push Lehman into bankruptcy. And while published reports have suggested that derivatives were at least partly responsible for the recent bankruptcies of forest products company **AbitibiBowater**, real estate investment trust **General Growth Properties** and Chrysler, market observers said it remains to be seen whether the influence of the contracts on future cases can be predicted with any degree of reliability.

"The impact of CDS on bankruptcy is still murky," said James Wehner of Washington-based law firm **Caplin & Drysdale**. "While in theory a creditor could completely decouple itself from its usual interests in an insolvency situation using CDS, under current disclosure rules, it's hard to demonstrate that it actually happens with any frequency."

Richard Metcalfe, global head of policy for the International Swaps and Derivatives Association (ISDA), noted that most investors use CDS to mitigate risk by reducing their exposure to a given credit. This reduces the investor's long position, but does not create the net short position that can skew motivation and disrupt a bankruptcy.

Further, building up such a short position via CDS becomes hugely expensive as a company approaches default. The price dynamic may act as a barrier to investors who would seek to use CDS to profit from a company's bankruptcy.

"It is a little naïve to suggest that someone can put on a net short position overnight," Metcalfe said.

Disclosure Sought

All sides agree that the CDS market will be more transparent in the future. "Every expectation is that increased disclosure and transparency will come in at some point," Metcalfe said. "We are not opposed to that."

Improved disclosure of CDS positions is seen as a key to managing the derivatives' disruptive effects on corporate bankruptcies.

The ISDA has advocated industry-developed transparency initiatives for the CDS market. Those would require less transparency in many cases than is seen in other securities and futures markets.

"The key questions are what is the information needed to be known, to whom, and when?" Metcalfe said. "You need to be careful" that the ability to conduct a trade is not impaired by mandatory disclosure, he said.

Metcalfe drew up a hypothetical example of a portfolio manager who holds $1 million of Company X loans and uses the CDS market to reduce his exposure to the credit by $400,000. This investor would still have a net long position of $600,000. Therefore, his economic interests would be aligned with the company's with regard to staying out of bankruptcy. In this case, the only effect of mandatory disclosure would be to provide an informational advantage to the investor's trading partners.

While new standards for CDS disclosure are debated, the mammoth Lehman bankruptcy is expected to establish legal precedent for future cases.

Claim Date

According to Steptoe's Lovi, a key juncture in the Lehman case will be when holders of CDS file claims (the

U.S. claim date has not been set). This will be followed by rounds of litigation from creditor committees, who will argue that losses are less than claimed. Litigating a few of the larger claims should establish benchmarks for valuations and preclude the need to litigate all claims.

Lovi said that one important aspect to the Lehman case will be whether contract counterparty disputes that have been resolved outside bankruptcy court will be taken into consideration, or if such previous cases will be judged as not relevant in a bankruptcy context.

Also, there are sure to be battles between holders of different Lehman obligations. CDS counterparties should not expect kind treatment.

"There will be a lot of pressure put on those who have other kinds of [Lehman] debt to say CDS are responsible for a lot of the problems, and those claims should be knocked down significantly," said Lovi, who is representing a Korean company that is facing a $300 million loss from CDS counterparty exposure to Lehman.

Aside from Lehman, practitioners note that there are billions of dollars of **General Motors** CDS outstanding, and a GM bankruptcy would be a closely watched case to gauge the impact of CDS.

Still, without more rigorous CDS disclosure standards, "it's difficult to quantify the impact on any individual case or on the bankruptcy system overall," said Wehner of Caplan & Drysdale.

When the current bankruptcy cycle is fully played out, evidence may show that earlier concerns that CDS would prove to be a significantly disruptive force in bankruptcies were overblown. "My guess is that we will conclude that the potentially perverse effects of CDS, which I and others have written about, haven't been a major factor in most cases – although they may have caused problems in a few," said David Skeel of the University of Pennsylvania Law School.

Continued from front page

If Standard & Poor's is correct, over the next two years European companies will post the highest default rates since the end of World War II. The average default rate for European speculative-grade debt issuers over the past 15 years was 3.2%, Standard & Poor's said in a recent report.

On the brighter side, "we have a lot of successful restructurings ahead of us," Le Berre said.

Historically, European nations adopted their insolvency laws to provide a mechanism for liquidating failed companies. Until the last few years, the laws didn't offer much flexibility to save a company through restructuring, even if most of the creditors agreed with the owners that a turnaround was the best option.

That's changing, as European politicians come to appreciate that saving a company also saves jobs. But the panelists warned investors coming to Europe not to expect a legal framework like Chapter 11 of the U.S. Bankruptcy Code.

"Local, national insolvency laws, as well as European regulation, rule," Le Berre said. "But these have been modernized a lot in the past two years. They now make it much easier to restructure successfully for all the stakeholders."

In fact, Lynn Hiestand, who co-leads the European corporate restructuring practice for the law firm **Skadden, Arps, Slate, Meagher & Flom** in London, warned them not to expect anything to be exactly the same.

"Don't assume that what works for you somewhere else, works in Europe," she said.

Hiestand said that the law in the United Kingdom that applies to corporate restructuring has changed for the better in recent years and other countries have "made great strides" but there are still a lot of important legal tools that aren't yet available to help turn around a company in Europe.

However, for European companies that need to restructure, the U.K. is "still viewed as the most hospitable jurisdiction," she said

The U.K. still has no dedicated insolvency procedure for restructuring financially distressed companies, Hiestand said. The two options available to avoid "administration" – which often ends up in a straightforward liquidation – are "schemes of arrangement" and "company voluntary arrangements" (CVAs), she said. Both contain weaknesses, Hiestand said.

As a result, more than 80% the restructurings that take place in Britain are handled outside a formal court-ordered process and without any predictable legal framework, Hiestand said.

The good news is that the U.K. government has announced that it will consider proposals to reform Britain's insolvency laws.

The government will "consult" on a proposal that will allow new funding for companies in restructuring similar to debtor-in-possession financing under U.S. bankruptcy law. The consultation is essentially a procedure where interested parties are invited to offer their opinions on a proposed new law or policy. The consultation on funding for insolvent companies will also include a proposal to broaden the moratorium on creditors taking action to collect on a debt while a business is trying to restructure under a company voluntary arrangement.

The moratorium is already available to small companies. The proposal under consideration would extend it to medium size and large companies.

Insolvency professionals who follow U.K. legislation closely warn against making any bets as to what happens next.

However, both of Britain's major political parties, Labor and the Conservatives, have publicly accepted the need for reform and modernization of the U.K.'s insolvency laws.

The party now in power, Labor, has instructed the government's Insolvency Service to begin consultation on reform of the nation's laws.

At the same time, there is a growing possibility that the Conservative Party will win the next general election and form the new government. If anything, that might accelerate modernization of Britain's insolvency laws.

David Cameron, the leader of the Conservative Party, gave a speech last summer in which he announced that if his party wins the next general election it would adopt in the U.K. many of the provisions of Chapter 11 of the U.S. Bankruptcy Code.

Specifically, he supported a short-term automatic stay of actions to collect on defaulted debt from all companies regardless of size, priority status for lenders providing funding to help reorganization and measures to prevent parties with no meaningful stake in a company's rescue from "holding up" the reorganization proceedings.

A powerful trade organization, the European High Yield Association (EHYA), has taken up the cause of arguing for new insolvency laws that open the door to rescuing companies rather than liquidating them. After briefly celebrating the Labor government's moves toward modernizing the insolvency laws, the association has started pressing to take the process further.

"On the whole, these initiatives are welcome, but they're really just a step down a road going in the right direction," said Gilbey Strub, managing director of the EHYA. "We would encourage the government to travel a little farther down the road."

Specifically, the association wants the U.K. to consider adopting more of the tools provided under Chapter 11 of the U.S. Bankruptcy Code, particularly legal mechanisms for resolving valuation disputes and modifying the rights of secured creditors.

Experts also agreed that further modernization of the insolvency laws in Germany, Europe's largest economy, would benefit creditors, investors, company owners and employees.

Kolja von Bismarck, a corporate restructuring specialist with the **Clifford Chance** law firm in Frankfurt, said Germany has been moving toward reforms that make the turnaround of a troubled company more likely. But he said the progress has been slow.

There are three, big shortcomings, he said, to German insolvency law: There is no provision for debt-for-equity swaps, creditors don't have the legal right to propose company officers to the court supervising an insolvency and no legal procedures exist for pre-packaged insolvencies.

Also, he said anyone planning to work on restructuring in Germany should become familiar with the criminal liability for failing to report "legal over-indebtedness."

Upon the occurrence of legal over-indebtedness, a company's management must file a report with the German government within 21 days. Failure to comply exposes the management to both personal civil and criminal liability.

Von Bismarck recommended that newcomers to business in Germany "take possession of some advice."