Lowenstein Sandler's Insurance Recovery Podcast: Don't Take No For An Answer

Episode 13 -
The Intersection of Insurance and Bankruptcy – Part 1

By Michael Lichtenstein and Joseph M. Saka
Guest: Jeffrey Cohen

APRIL 2021

Kevin Iredell: Welcome to the Lowenstein Sandler podcast series. I'm Kevin Iredell, Chief Marketing Officer at Lowenstein Sandler. Before we begin, please take a moment to subscribe to our podcast series at lowenstein.com/podcasts. Or find us on iTunes, Spotify, Pandora, Google podcast, and SoundCloud. Now let's take a listen.

Michael Lichtenstein: Good morning everyone and welcome to this episode of "Don't Take No for an Answer", an Insurance Recovery podcast.

This is Michael Lichtenstein, your host for today, but I'm really excited about today's podcast because it's our first one where I actually get to have a guest host, which means I don't have very much to do today. I'm pleased to introduce to you all my friend and colleague Joe Saka. He's a Senior Counsel at Lowenstein in our Insurance Recovery Group. He works out of our DC office and he's going to be doing most of the questioning today and he will introduce our guest in a more fulsome way in a minute. But I just want to say hi to Jeff Cohen also my friend and colleague. Jeff is Chair of Lowenstein's very prestigious Bankruptcy Group. And he's generously agreed to spend some time with us to talk about bankruptcy and its intersection with insurance. With that as background, Joe, take it away.

Joseph Saka: All right. Thank you very much, Michael, for that introduction. And Jeff, thanks very much for being here. I wanted to give our audience a brief summary of your background. Jeff is most well-known for representing creditors' committees in retail and distress technology cases. He's served as lead counsel to the official committee of unsecured creditors in some of the most prominent retail bankruptcy cases in the country, including for example, Gibson Guitar, Brookstone, Blockbuster and the Sharper Image. He also represents individual creditors, including most notably Under Armour, Estee Lauder, Fila, Columbia and the National Football League. Some of his current representations include the creditors' committees in GNC, Century 21 and Modell's Sporting Good. His practice also centers on working with private equity sponsored and venture capital backed distressed companies and on representing boards of directors at management in out of court wind downs and distressed M and A processes.

Earlier this year, he was appointed chair of Lowenstein's bankruptcy and restructuring department, which the Wall Street Journal has called one of the nation's power players in large corporate bankruptcies. With that introduction, Jeff, thank you for being here. Anything you want to add to that background?

Jeffrey Cohen: Other than that it's mildly embarrassing. No, thanks for having me. I appreciate it.

Joseph Saka: Thank you. I kind of wanted to get started with some of your background and how you went from presumably a junior associate at one point to chair of Lowenstein's bankruptcy group. How did you get started at bankruptcy law?

Jeffrey Cohen: I went to law school at St. John's Law, where I was an editor on the American Bankruptcy Institute Law Review, which was basically the number one law review in the country that's focused on bankruptcy law. When I was applying for first year associate positions at law firms in New York City, seeking a litigation spot, a rather prominent law firm made me an offer, but said, "We don't want you for litigation. We only want you for bankruptcy." I figured I would start there as it was probably the best firm I could ever find and if I didn't like bankruptcy, I can pivot to another department or pivot to another firm. 21 years later, I'm still doing bankruptcy. I thank them for making that decision for me.

Joseph Saka: Right. And I guess that raises the question, what's kept you there for so long?

Jeffrey Cohen: I still in my heart of hearts view myself as a litigator and that's where it really excites me to go to work every day. For those of you who have participated in any bankruptcy case, it's really like litigation for people with immediacy issues, which is right up my alley. We're not going to litigate any issue for two to four years. We'll be soup to nuts in two to four months. That's perfect for me. In the end, I ended up getting what I wanted, being in court as often as possible, litigating contentious disputes, but going from beginning to end with much more speed.

Joseph Saka: And how did you come to specialize or spend most of your time representing creditors' committees?

Jeffrey Cohen: After I spent a few years at my first law firm, which was Simpson Thatcher and Bartlett, I transferred over to a boutique New York City law firm. And by boutique, I meant 90 lawyers, called Kronish Lieb Weiner and Hellman which ultimately merged into Cooley, the New York office of Cooley to this day. And their specialty at Kronish Lieb was creditors committee in the retail space. I just really took to it. I was raised in retail. I got my first job at 14 stocking shelves in a supermarket. I worked my way through college as a manager of a sneaker store chain in upstate New York. I just understand retail from the consumer perspective, from the operations perspective and it just made sense marrying that with my legal career.

Joseph Saka: Yeah, I think that's a great segue to the last March and the start of the pandemic. And to preface it, I kind of remember just being pretty frightened by seeing stores kind of being forced to close for months at a time. And I think my expectation at that time was we were going to see a lot of companies have to file for bankruptcy and in some ways that's come to fruition. But what were your expectations at that time?

Jeffrey Cohen: Well, March and April last year were obviously chaotic for all of us on a personal level, but professionally was an absolute whirlwind for a restructuring professionals. To think that we would find ourselves in a situation where basically no one sitting around the table knew what to do or what the answer was, was very unsettling. Usually you find yourself in a distress situation, you've seen part of that play before or seen elements of it in other cases and you're guided by prior experiences. There was no prior experience in 21 years of practice that helped me in those first few months. In addition, one of my first new engagements post-COVID was representing the creditors committee in Modell's Sporting Goods. I worked at Modell's Sporting Goods 26 years ago. I was the manager of the footwear department when they were opening their Roosevelt Field location, as I entered into the law school.

For me, being able to work on the Modell's Sporting Goods bankruptcy case was somewhat, sort of full circle from my life experience. In addition, I represent a lot of footwear and apparel brands in sporting goods. Representing a committee full of the people I've come to represent professionally and trying to help them recover from a company that I used to work for as a kid, had a lot of attractiveness to it. And then I actually, am successful in getting the engagement and beating out my competitors to get the engagement and I can't even liquidate the stores because the stores can't open. It was pretty frustrating. Frankly, there were moments where we thought the case would have to either get dismissed or converted to Chapter 7 because they filed with the specific intention of going out of business and running store closing sales. They turned off their website prior to COVID happening and then couldn't close their actual stores because their actual stores were closed and couldn't liquidate their inventory online because they shut down on their website.

I just successfully got retained in a company that was very meaningful to me and for days or even the first few weeks, I actually thought we would lose the engagement because the case would go away. I thought we would just hand over the keys to the bank and say, "Here, liquidate the inventory when you can access it." We literally couldn't even access it. It's not like when COVID reopened in public spaces, we couldn't even take the inventory and put it in the middle of Giant Stadium and sell it in open air. We couldn't get into the stores to get it. We felt at least professionally a little helpless or without answers for those first few weeks. But like the rest of us, even in our personal lives, when we finally found the roll of toilet paper and some hand sanitizer, professionally we eventually found our footing and figured things out.

Joseph Saka: How did that issue get resolved?

Jeffrey Cohen: That was really our first taste of required collaboration and cooperation. Usually a bankruptcy case has an undertone of contentious relationships between the debtors and the committee. Because the debtors failed to pay all the people that are on the committee. Usually there's a little bit of an adversarial relationship between the debtors, the vendors and the lenders, because the lenders just want to get out of Dodge paid a 100%. This was really our first experience of there was no choice. We all had to get around the table together virtually and figure out a joint solution. It really wasn't about negotiating for your respective position and trying to leverage an advantage yourself. It was trying to find the best answer for all of you collectively. We really couldn't have done it without negotiating a solution with the landlords because we didn't pay rent while the stores were dark and under the bankruptcy code once you filed the bankruptcy case, and even obviously outside of bankruptcy, you're obligated to pay your occupancy costs, whether or not you're able to access the stores.

And obviously we'll get into this probably a little further on in this podcast, but there's an argument on the half of the tenant that if I can't access my stores as a result of a governmental order, does that constitute a force majeure or some exception to your lease where you can get excused from paying a rent? Well, the landlords argued that we owed them 100 cent rent for every month, even whether we were operating or not. We as a bankruptcy estate couldn't afford that. The gating issue to us even reopening the stores was reaching an accord with the landlords, which we ultimately had to do through mediation where another bankruptcy judge, actually our former partner, Jack Sherwood stepped in to mediate the dispute between the estates and the landlords.

And we ultimately agreed to pay them a percentage of what was owed so they would reopen and then agree to pay them a 100 cents going forward for every day that the stores were open and we reopened and managed to liquidate basically winter sporting goods in the middle of the summer and ultimately concluded those sales before the end of the summer of last year.

Joseph Saka: I suspect that while it was unique to that bankruptcy, you saw a lot of similar issues where there was a need to coordinate between retailers and landlords in several bankruptcies. Has that been the case? And has the number of bankruptcies surprised you in any way?

Jeffrey Cohen: Last year was very busy from a Chapter 11 filing perspective. Modell's Sporting Goods created a little bit of a template. Really it was really Modell's Sporting Goods and then shortly thereafter Pier One filed in the eastern district of Virginia, both of them really set the table for how to resolve the landlord issues for the months of dark rent. Once that issue sort of established a pattern very quickly, that no longer became a pressing issue in future cases last year. But the caseload, the volume of cases really continued from March through around November.

By that time, obviously retail was expecting to enter into what we all believed would be a historically bad holiday season. We thought that the holiday season

would be so historically awful that we would see a surge of filings in Q1 and Q2 of this year. The surprising thing became that those filings never happened. That obviously holiday season disappointed as expected. I don't think it was as disappointing as people feared, but still historically low, but it did not result in this mass wave of filings that we all expected to occur early this year. And that was surprising to us.

Joseph Saka: And what do you attribute that to?

Jeffrey Cohen: I've lived through a couple of bubble bursts in my career in bankruptcy, the tech bust in early 2000 post Lehman Brothers after 2008. And obviously COVID. After Lehman Brothers filed in 2008, there was a few years where bankruptcy was just smoking hot. It felt like was every day or every week, a new large company was filing for the purpose of liquidating. And eventually banks decided, I can't take another loss. I've taken too many losses this year. I can't liquidate another furniture store because they just liquidated six of them and the consumers already bought everything they need. If I would run another liquidation Now, my loss would be 60% instead of 20%. It makes sense if I just amend my loan agreement, extend this out another year, collect a fee in doing so and worry about this next year, where hopefully the company will stabilize or the economy will stabilize.

I think we're seeing some parallels here where banks are saying to themselves, "I'm faced with a couple of my portfolio companies that were otherwise performing very well pre-COVID. COVID's clearly the reason why they're not performing now. All we need to do is get them to the other end of this tunnel. If we can just bridge them to when COVID ends or consumers return to brick and mortar with some level of normalcy, then instead of taking a loss and liquidating now, I can have a profitable, stable relationship with a very well run and operating retailer on the other side of COVID."

I think the first few months of 2021, the companies that are in distress along with their banks and their boards of directors, were trying to make educated guesses on when consumer purchasing patterns will return to normalcy. And if they thought it was July 4th or Labor Day or holiday 2021, how much by way of funding will it take to get there? And then once they realized what the occupancy costs and operational costs would be, it's putting all those minds together, figuring out if they can find a source of funding to bridge the gap and then to see if they can get to the other end and restore themselves to normalcy and healthy operations.

And I think we've seen a lot of lenders ultimately decided they'd rather, if analysis economically made sense, to provide further funding to bridge the gap that it made sense for them to do so rather than taking a loss on a company that was otherwise very healthy pre-COVID. That was frankly surprising because we thought that some companies would have just such an awful, awful holiday season and with no sign of when things would return to normalcy that

interested parties would pull the plug. And just ultimately that hasn't happened. It was surprising and an interesting development from our perspective.

Joseph Saka: And I guess it's probably too soon to tell whether that bet for lack of a better word, from the lenders will pay off in the long run.

Jeffrey Cohen: Yeah, I think you'll see it in tranches. I assume with some companies, the lender said, "Well here, I'll fund you through back to school. And if back to school ultimately shows that it's profitable, then we'll roll through holiday and we'll do that outside of a process, without filing chapter 11. But if back to school is 20% below year over year from 2019," you won't use 2020, you'll use 2019 for comparison purposes, "then we'll file in October and we'll liquidate during the holiday season, which is the most profitable time of year liquidating."

Other retailers with their lenders probably looked at how much it would cost to get through the entire year and say, "Well, we'll try back to school and holiday." I think you'll see a little bit of a mix. We might see, I won't call it a surge or a wave, but you might see an uptick in filings in October for companies that underperformed in back to school, by such a level that lenders are not interested in trying out the holiday season or are interested in using holidays for the purpose of liquidating. And others will just be having the same conversation next January to see whether they decide to pull the plug.

Joseph Saka: Fascinating. And I'm sure we could keep going on this topic.

Michael Lichtenstein: Jeff and Joe, thanks so much. This has been really interesting. There's so much content here that we're going to break this discussion up into two separate podcasts. This will be the end of podcast number one and we look forward to hearing you all for podcast number two coming shortly. Thanks for listening.

Kevin Iredell: Thank you for listening to today's episode. Please subscribe to our podcast series at lowenstein.com/podcasts, or find us on iTunes, Spotify, Pandora, Google podcasts, and SoundCloud. Lowenstein Sandler podcast series is presented by Lowenstein Sandler and cannot be copied or rebroadcast without consent. The information provided is intended for a general audience. It is not legal advice or a substitute for the advice of counsel. Prior results do not guarantee a similar outcome. The content reflects the personal views and opinions of the participants. No attorney client relationship is being created by this podcast and all rights are reserved.