

Chicago Daily Law Bulletin®

Volume 162, No. 9

Serving Chicago's legal community for 161 years

Kirkland team shelters \$1.4B in bankruptcy duel

Looking to make Chapter 11 proceeding work as it should, McGaan saves value for case's creditors

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In a popular Texas saying, size can be exaggerated. But in the bankruptcy case of Dallas-based Energy Future Holdings, the phrase held true — everything about it is big.

EFH's 2007 creation was the largest leveraged buyout of all time, valued at \$32 billion. By the time of its 2014 Chapter 11 bankruptcy filing, the power plant operator and energy supplier was saddled with roughly \$42 billion in debt. The Wall Street Journal called it the eighth largest bankruptcy in U.S. history.

EFH, which hired Kirkland & Ellis LLP as its lead bankruptcy adviser, is among the largest corporate flameouts in American history. But Andrew R. McGaan's story showed that even in failure there can be victory.

A Chicago-based Kirkland litigation partner, McGaan successfully defended an EFH subsidiary — or, in bankruptcy parlance, a debtor — against \$1.4 billion worth of creditors' claims.

In doing so, McGaan and his team of litigators helped smooth the road to a bankruptcy plan that was approved last month by U.S. Bankruptcy Judge Christopher S. Sontchi for the District of Delaware.

By extinguishing the \$1.4 billion in claims, McGaan and his co-lead counsel, San Francisco-based Mark E. McKane, helped preserve value in the EFH bankruptcy which could be distributed to satisfy a broader set of creditors.

"Value is the juice that helps drive all these restructuring plans," McGaan said. "If the value gets drained out in favor of one creditor, there is less opportunity to find agreement among the rest."

McGaan's litigation team involved more than 50 lawyers. He personally spent more than 3,000 hours on EFH bankruptcy litigation over two years.

While compromise is an essential component of bankruptcy proceedings, litigation arises when an indebted company and a lender cannot reach common ground.

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The first battle arose shortly after EFH's April 2014 bankruptcy filing. A group of creditors sought to relocate the bankruptcy from Delaware to Dallas. The judge ruled in favor of EFH and, for



Andrew R. McGaan

McGaan, it was the first of three trial victories over the course of the litigation.

A second trial victory was over a plan for the management of EFH and corresponding compensation. The final trial victory came after 10 days of hearings in November that culminated in Sontchi's ruling to approve the EFH bankruptcy plan. The plan still awaits Texas state regulators' approval.

Sandwiched between those trials, McGaan's team earned a series of favorable summary judgments that wiped out \$1.4 billion in potential payments to three layers of creditors.

Energy Future Intermediate Holdings LLC, an EFH subsidiary, had agreed to pay off loans from these creditors, McGaan said, but the two sides came to loggerheads over interest payments.

The first tier of creditors, which were owed about \$4 billion, argued for an extra \$431 million in interest. The second layer, which were owed about \$2.2 billion, made a claim worth \$400 million of forgone in-

terest payments. And lastly, a group of unsecured creditors owed about \$1.6 billion sought \$113 million in interest.

The creditors argued those dollar amounts were the value of "make-whole" agreements in their loans. The make-whole agreements were essentially a guarantee that if the high-yield loans were paid off early they would still include interest payments set to be paid over the full duration of the loan.

"The creditors said, 'We have the right to get the interest you would have paid us if you left this loan in place for the next five years. We expected this high-yield return. We want the net present value,'" McGaan said. "It's a common provision in high-yield debt instruments. But it's a whole different animal when you repay a loan in bankruptcy."

Starting with a summary judgment ruling on July 8, McGaan's team won a clean sweep as the judge found one by one the creditors were not owed the make-whole payments, which totaled roughly \$940 million.

There was one more battle, worth \$460 million, over a claim for post-petition interest by the third tier of creditors. When EFH won that, McGaan's litigation efforts had secured \$1.4 billion in value that would eventually be distributed to a broad set of creditors.

"All of that together, was the end result of using litigation to preserve value," McGaan said. "It gave (the bankruptcy lawyers) more tools to work with in trying to craft a deal."

The deal Kirkland's team structured, which includes a plan to sell the EFH subsidiary to pay off a large portion of EFH's debt, earned high praise from the judge.

"This is exactly the type of practical business solution to insolvency that Chapter 11 is designed to foster," Sontchi said at the Dec. 3 confirmation hearing. It "showcases the benefits of the flexible, if often expensive, Chapter 11 process."

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