A MARKET BASED THEORY TO DEMONSTRATE LACK OF REASONABLY EQUIVALENT VALUE FOR ABUSIVE DEBT EXCHANGE OFFERS

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IV. Conclusion

INTRODUCTION

"[I]t looks like the reasonable commercial expectations of the lenders participating in this arrangement is being undermined by some of the lenders getting together and saying look, if we don't tell the other guys what we're doing, we can cut them out of the picture. It doesn't seem very fair."

— Transcript of the Proceeding at 21, *Octagon Credit Investors, LLC v. NYDJ Apparel, LLC*. Index No. 6566677/2017 (NYECF Doc. No. 91) (N.Y. Sup. Ct. March 27, 2018) ("*NYDJ*")

"The Parties have not cited, and the Court has not found, any case in which a no-action provision was strategically deployed in the manner alleged here—by a subset of lenders, without notice or consent, as part of a larger scheme to breach and then exit the agreement. The amended no-actions were, according to Plaintiffs, purpose-built to prevent these Plaintiffs from suing these Defendants in connection with this transaction—a preemptive self-pardon, of sorts. Subtle, this was not."

— Decision and Order at 16, *Audax Credit Opportunities Offshore Ltd., et. al. v. TMK Hawk Parent, Corp, et. al.*, Index No. 565123/2020 (NYECF Doc. No. 171) (N.Y. Sup. Ct. August 16, 2021) ("*TriMark*")

"Elbows are getting sharper out there . . . Credit-Market Clashes are Getting Uglier, Dirtier, More Common here."

— Weekly News — May 13, — Creditor Rights Coalition: Creditor Corner (May 13, 2022), https://creditorcoalition.org/weekly-news-may-13/

During times of severe financial distress, such as the weakness of the price of oil from 2015 to 2020, the COVID-19 pandemic, and the war in Ukraine, many over-leveraged companies structure liquidity events with a select group of lenders to try to stave off bankruptcy. Certain liability management transactions, or "uptier" public debt exchange offers, have become all the rage. These "uptier exchanges" are the newest way for companies in financial distress to manage their liabilities by allowing consenting lenders to exchange their term loans for newly issued term loans under superpri-

ority term loan facilities, pitting one lender group against another. Harmed lenders have called these deals a "cannibalistic" assault, or "lender-on-lender violence," and have tried to enjoin them, reverse them, or seek damages on a number of grounds, asserting breach of contract, self-dealing, tortious interference with contract, bad faith, breach of fiduciary duty, or intentional fraudulent transfer.[1]

This article describes a market based theory to challenge "uptier exchange" public debt exchange offers[2] as constructive fraudulent transfers when an issuer is insolvent, asserting that the issuer does not receive reasonably equivalent value if the market value of the new debt received by the lenders ("New Debt") is greater than the trading or quoted value of the existing debt exchanged ("Old Debt").[3] This is because the principal amount of the Old Debt during insolvency is not its fair market value. Simply put, the holders of the Old Debt will not receive face value in a subsequent bankruptcy, and the estate will be depleted. The authors are not aware of case law directly addressing an application of this theory; however, this theory is consistent with sound principles of finance reflecting the time value of money, the relationship between risk and return, and the probability the exchanged debt will be paid at maturity. The general principles that underlie this theory are supported in case law, including use of fact inten-

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[1] See extensive discussion of common legal attacks of these abusive transactions in Shana A. Elberg, Evan Hill, Catrina A. Shaw, Uptier Exchange Transactions Remain in Vogue, Notwithstanding Litigation Risk, Skadden, Arps, Slate, Meagher and Flom, LLP (February 2, 2021); Diane Lourdes Dick, Hostile Restructurings, 96 Wash. L. Rev. 1333 (2021); Linda Filardi et al., Erosion in Creditor Remedies in Loan Documentation and Lessons from TriMark, LSTA, (October 21, 2021). Another apt term is "Bankruptcy Hardball." Jared A. Ellias & Robert Stark, Bankruptcy Hardball, 108 Cal. L. Rev. 745–88 (2020).

[2] Uptier exchanges, whereby noteholders exchange unsecured notes into new secured notes, is a commonly used structure. See Dustin Mondell and Simone Bono, Selected issues in high yield bond restructurings in Europe: Overview of coercive exchange offers, Debtwire European Forum (2015).

[3] The circumstances under which such exchange offers might also constitute intentional fraudulent transfers are beyond the scope of this article. One recent intentional fraudulent transfer action was dismissed on jurisdictional grounds. See Decision and Order at 33–37, Audax Credit Opportunities Offshore Ltd., et. al. v. TMK Hawk Parent, Corp, et. al., Index No. 565123/2020 (NYECF Doc. No. 171) (N.Y. Sup. Ct. August 16, 2021).

sive, totality of the circumstances analyses and consideration of the net effect on an insolvent entity.

I. What is an Abusive Debt Exchange?

A. General Rules

Lenders who are left out of an uptier exchange and wish to challenge the exchange as a fraudulent transfer may allege both actual fraud and constructive fraud. Allegations of actual fraud require the plaintiff to show that the uptier exchange was made "with actual intent to hinder, delay, or defraud any creditor of the debtor."[4] Although certain "badges of fraud" may be considered in determining fraudulent intent, it is unlikely that a creditor will find clear evidence of actual fraud, especially when debtors are sophisticated financial entities. That is why this article focuses primarily on constructive fraud.

Disgruntled creditors outside of bankruptcy are limited to state fraudulent transfer laws, but once a bankruptcy petition is filed, the fraudulent transfer provisions of the Bankruptcy Code[5] also become available. Bankruptcy trustees, debtors in possession (DIPs), and creditors with derivative standing[6] have two avenues in attempting to avoid a transfer as constructively fraudulent on behalf of the bankruptcy estate: section 548 of the Bankruptcy Code, on the one hand, and state fraudulent transfer law, on the other. Bankruptcy Code section 548 deems any transfer of an interest of the debtor in property or any obligation incurred by the debtor that was made or incurred within two years before the petition date to be constructively fraudulent and avoidable if, in pertinent part,(i) the debtor received "less than a reasonably equivalent value in exchange for such transfer or obligation" and (ii) the debtor was insolvent when the transfer occurred or became insolvent as a result of the transfer, was unreasonably undercapitalized, or intended to incur debts beyond its

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[4] Uniform Voidable Transactions Act (UVTA) § 4(a)(1).

[5] 11 U.S.C.A. § 101 et seq. (the "Bankruptcy Code").

[6] See generally Derivative Standing in Chapter 11, Practical Law Practice Note w-017-9721 (explaining how a creditor or creditors' committee may bring fraudulent transfers under the Bankruptcy Code on behalf of the DIP or Trustee).

ability to pay upon maturity of those debts.[7] Likewise, under Bankruptcy Code § 544(b), fraudulent transfers can be avoided under a similar analysis pursuant to applicable state fraudulent transfer laws.[8] As of 2022, 45 states, in addition to the U.S. Virgin Islands and the District of Columbia, have adopted the Uniform Law Commission's Uniform Fraudulent Transfer Act (the "UFTA") or its successor, the Uniform Voidable Transactions Act (the "UVTA" and, with the UFTA, the "Uniform Act").[9] The Uniform Act in many respects parallels § 548, although the laws are not identical. For instance, while the Bankruptcy Code's § 548 allows a trustee to avoid only transactions made within two years of the bankruptcy case's petition date, the Uniform Act's § 9 allows a plaintiff to bring an avoidance claim up until four years after the transfer (or one year after the transfer was or could have been reasonably discovered, whichever is later). When analyzing constructive fraud under the Uniform Act, courts again look at whether the transfer was made "without receiving a reasonably equivalent value" as well as whether the debtor was engaging in business for which the remaining assets were unreasonably small or intended to incur debts beyond the debtor's ability to pay as they came due.[10]

In uptier exchanges, the issue of reasonably equivalent value is increasingly important, more so than the question of incurring liabilities beyond the ability to pay. After all, debtors engaging in such exchanges can argue that they are intending to stay afloat, not further their financial woes. Our focus thus turns to an analysis of whether a given debtor

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[7] See 11 U.S.C.A. § 548(a)(1).

[8] See 11 U.S.C.A. § 544(b). Under Bankruptcy Code section 550, to the extent a transfer is avoided under Bankruptcy Code sections 548 or 544, the debtor in possession (or another party with requisite standing) may recover, for the benefit of the estate, the property transferred or, if the court so orders, the value of such property.

[9] Alaska, Louisiana, Maryland, Puerto Rico, and Virginia have never adopted Uniform Fraudulent Transfer Act (UFTA) or UVTA. South Carolina, which did not adopt UFTA, has bills in both its State Senate and State House of Representatives to adopt UVTA. SB 0262 (2019); HB 4390 (2022).

[10] UVTA § 4 (granting an avoidance cause of action to both present and future creditors with relation to the time of the disputed transaction or obligation); see also UVTA § 5 (granting another avoidance cause of action only for present creditors).

received "reasonably equivalent value" in exchange for issuing the new debt.

B. Distressed Debt Exchanges

Companies are often faced with untenable capital structures, which can result in (i) their liabilities being greater than the value of their assets, (ii) the inability to pay their debts as they come due, or (iii) inadequate capital to operate their businesses. Such distressed companies have multiple options to choose from to address their unsustainable capital structures, including filing for bankruptcy, conducting an out-of-court restructuring to extend maturities or obtain covenant relief, or pursuing a distressed debt exchange.

Exchange offers have been a common out-of-court restructuring tool for decades, variously described as "workouts," "up the ladder offers," and, currently in vogue, "uptier exchanges." Exchange offers are uptier when creditors are asked to swap Old Debt for New Debt with not only different characteristics, such as interest rate, PIK interest, maturity date and financial covenants, but also collateral or priority enhancements. While the New Debt might have a lower principal face amount, it sits higher up in the capital stack vis à vis the Old Debt. These uptier exchanges may also be accompanied by proposals to strip covenants out of the Old Debt, thereby devaluing the Old Debt for those that choose not to exchange or, more likely, were not offered the opportunity to exchange. The New Debt is generally offered at a premium over the fair market value of the Old Debt, which is probably trading at a significant discount—these are called "Fair Value Exchanges." The exchange results in an overall reduction in the face value of the issuer's outstanding debt. The holders of the New Debt, however, have improved the fair market value of their positions, while the legacy holders of the Old Debt (or perhaps other debt) see a loss. This article focuses on these uptier debt exchanges.[11]

Distressed debt exchange offers become more common during times of financial distress. During the financial crisis in 2008, for example, there was a significant uptick in distressed

[11] Debt exchange offers that do not reduce principal, so-called Face Value Exchanges, and cash exchange offers, are outside the scope of this article.

exchanges as indicated in the chart below.[12] One of the earliest uptier transactions was Not Your Daughters Jeans ("NYDJ") on May 25, 2017.[13] There have been several others since then.[14]

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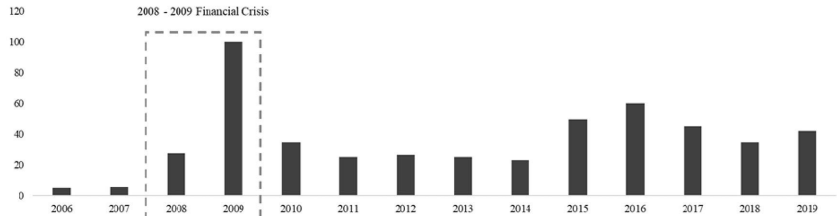
[12]Distressed exchanges will likely rise in tandem with corporate defaults, Moody's (Mar. 27, 2020) https://www.moodys.com/research/Default-Trends-Global-Distressed-exchanges-will-likely-rise-in-tandem—PBC_1220828.

[13]NYDJ, or Can You Really Prime 47% of Lenders Without Their Consent? King & Spalding https://www.kslaw.com/attachments/000/008/524/original/How_did_they_do_it_NYDJ.pdf?1611586634.

[14]Bek R. Sunuu, A Closer Look At How Uptier Priming Loan Exchanges Leave Excluded Lenders Behind S&P Global (June 15, 2021) https://www.spglobal.com/ratings/en/research/articles/210615-a-closer-look-at-how-uptier-priming-loan-exchanges-leave-excluded-lenders-behind-11991317.

Graph 1 — The Number of Distressed Debt Exchanges Increased During the Last Financial Crisis



The relative weakness in the price of oil since 2015 and other causes have resulted in many distressed debt exchange offers in the oil exploration and production ("E&P") industry over the last several years. Between January 2015 and February 2016, there were eight completed domestic E&P distressed exchanges.[15] Many of the debt exchange offers were initiated when the issuers were insolvent and were alleged to have been abusive to junior creditors. All eight of these exchanging issuers subsequently filed for bankruptcy, some within a year of completing the transaction.

Table 1 — Subsequent Bankruptcies for Oil Exploration & Production (E&P) Domestic Exchanges

#	Company	Exchange Offer Settlement Date	Date of Subsequent Bankruptcy	Days Between Exchange Offer and Bankruptcy	Unsecured Note Recovery	Secured Debt Recovery
1	Venoco Inc.[16]	4/2/2015	3/18/2016	351	2.0 — 4.0%	0.0% — 6.0%
2	Midstates Petroleum Company[17]	5/21/2015	4/30/2016	345	0.5% — 0.9%	7.8%
3	American Energy — Woodford, LLC[18]	6/24/2015	5/28/2016	1,433	0.3%	Redeemed prior to bankruptcy

[15] Distressed Exchanges Remain Frequent Thanks to Oil and Gas, PE Firms, Moody'S (Nov. 17, 2015).

[16] Venoco Inc., Current Report (Form 8-K) (Apr. 8, 2015); Disclosure Statement at 19, In re Venoco., Case No: 16-10655-KG (Docket No. 221) (Bankr. D. Del. May 17, 2016).

[17] Midstates Petroleum Company, Current Report (Form 8-K) (May 22, 2015); Disclosure Statement 19-20, In re Midstates Petroleum Company, Case No: 16-32237 (Docket No. 382) (Bankr. S.D. Tex. July 13, 2016).

[18] American Energy — Woodford, LLC Announces Significant Balance Sheet Enhancement That Increases Invested Equity By $100 Million, Reduces Debt By $152 Million And Increases Liquidity By $171 Million PR Newswire (June 25, 2015) https://www.prnewswire.com/news-releases/amer

#	Company	Exchange Offer Settlement Date	Date of Subsequent Bankruptcy	Days Between Exchange Offer and Bankruptcy	Unsecured Note Recovery	Secured Debt Recovery
4	Goodrich Petroleum Corporation[19]	10/1/2015	4/15/2016	197	0.0%	22.0%
5	EXCO Resources[20]	10/19/2015	1/15/2018	819	23.0%	23.0%
6	Warren Resources[21]	10/22/2015	6/2/2016	224	2.9%	2.9%
7	Halcon Resources Corporation[22]	12/21/2015	8/7/2019	1,325	22.1%	Redeemed prior to bankruptcy

ican-energy——woodford-llc-announces-significant-balance-sheet-enhancement-that-increases-invested-equity-by-100-million-reduces-debt-by-152-million-and-increases-liquidity-by-171-million-300105236.html; Disclosure Statement at 13, In re White Star Petroleum Holdings, LLC, Case No: 19-12521 (Docket No. 1008) (Bankr. W.D. Okla. February 11, 2020) (second lien notes were fully redeemed in late 2015 and through 2016 in a series of equity and cash transactions.).

[19]Goodrich Petroleum Corporation, Current Report (Form 8-K) (Oct. 2, 2015); First Amended Complaint at 4, In re Goodrich Petroleum Corporation, Case No. 16-31975 (Docket No. 15) (Bankr. S.D. Tex. January 6, 2017).

[20]EXCO Resources, Current Report (Form 8-K) (Oct. 21, 2015); Disclosure Statement at 206, In re Exco Resources, Case No: 18-30155 (Docket No. 1907) (Bankr. S.D. Tex. May 3, 2019).

[21]Warren Resources, Current Report (Form 8-K) (Oct. 22, 2015); Disclosure Statement at 34 In re Warren Resources, Case No. 16-32760 (Docket No. 114) (Bankr. S.D. Tex. June 20, 2016).

[22]Halcón Resources Announces Expiration and Final Results of Debt Exchange Offer, GLOBENEWSWIRE (Dec. 18, 2015) https://www.globenewswire.com/fr/news-release/2015/12/18/797013/0/en/Halc%C3%B3n-Resources-Announces-Expiration-and-Final-Results-of-Debt-Exchange-Offer.html; Disclosure Statement at 15, 24 In re Halcon Resources Corp., Case No. 19-34446 (Docket No. 19) (Bankr. S.D. Tex. August 7, 2019) (second lien notes were redeemed in 2017 as a part of an asset divestiture.).

#	Company	Exchange Offer Settlement Date	Date of Subsequent Bankruptcy	Days Between Exchange Offer and Bankruptcy	Unsecured Note Recovery	Secured Debt Recovery
8	Vanguard Natural Resources[23]	2/10/2016	2/1/2017	357	12.6%	100%

Since 2018, Ultra Petroleum Corporation ("Ultra"), EP Energy Corporation, Denbury Resources Inc., Chesapeake Energy Corporation ("Chesapeake"), SM Energy Corporation, and Transocean Ltd have completed uptier debt exchanges. Four of these six companies subsequently filed for bankruptcy, including Ultra for the second time.[24]

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[23]Vanguard Natural Resources Announces Expiration and Final Results of Offer to Exchange Any and All Outstanding Senior Notes Due 2020 for New Senior Secured Second Lien Notes Due 2023, GlobeNewswire (Feb. 8, 2016) https://www.globenewswire.com/news-release/2016/02/08/808557/34714/en/Vanguard-Natural-Resources-Announces-Expiration-and-Final-Results-of-Offer-to-Exchange-Any-and-All-Outstanding-Senior-Notes-Due-2020-for-New-Senior-Secured-Second-Lien-Notes-Due-20.html; Disclosure Statement at 33 In re Vanguard Natural Resources, LLC, Case No. 17-30560 (Docket No. 892) (Bankr. S.D. Tex. October 19, 2020).

[24]In connection with the second Ultra bankruptcy, Teneo represented the Official Committee of Unsecured Creditors, which requested standing to challenge the Ultra Debt Exchange. The Official Committee of Unsecured Creditors in Ultra ultimately reached a settlement with Ultra and other constituents with respect to the Ultra Debt Exchange and Ultra's plan of reorganization. On August 22, 2020, the Court entered an order confirming Ultra's plan of reorganization. Order Approving Disclosure Statement, In re Ultra Petroleum, Case No: 20-33631 (Docket No. 736) (Bankr. S.D. Tex. August 22, 2020).

Table 2 — Oil Exploration & Production (E&P) Domestic Exchanges — Jan. 2018 to Dec. 2020

#	Company	Exchange Offer Settlement Date	Date of Subsequent Bankruptcy	Days Between Exchange Offer and Bankruptcy	Unsecured Note Recovery	Secured Debt Recovery
1	EP Energy Corporation[25]	1/3/2018	10/3/2019	638	3.5%	15.1%
2	Ultra Petroleum Corporation[26]	12/21/2018	5/14/2020	510	1% — 4.7%	4.0%
3	Denbury Resources Inc.[27]	6/17/2019	7/30/2020	409	0.0% — 1.2%	61.5%
4	Chesapeake Energy Corporation[28]	12/19/2019	6/28/2020	192	2.3% — 4.1%	[+80%]

[25]EP Energy Corporation, Current Report (Form 8-K) (Jan. 4, 2018); Fourth Amended Disclosure Statement at 27–28, In re EP Energy, Case No: 19-35654 (Docket No. 686) (Bankr. S.D. Tex. January 13, 2020).

[26]Ultra Petroleum Corporation, Current Report (Form 8-K) (Dec. 21, 2018); Disclosure Statement at 15 In re Ultra Petroleum, Case No: 20-32631 (Docket No. 18) (Bankr. S.D. Tex. December 18, 2020).

[27]Denbury Resources, Current Report (Form 8-K) (June 17, 2019); Disclosure Statement at 18, In re Denbury Resources, Case No: 20-33801 (Docket No. 17) (Bankr. S.D. Tex. July 30, 2020).

[28]Chesapeake Energy Corporation, Current Report (Form 8-K) (Feb. 9, 2021); Fifth Amended Plan at 21–25 In re Chesapeake Energy, Case No: 20-33233 (Docket No. 2833) (Bankr. S.D. Tex. January 12, 2021). In December 2019, Chesapeake entered into a number of refinancing transactions whereby approximately $2.2 billion of new second lien debt was issued in exchange for existing unsecured notes, at a discount (the "CHK Debt Exchange"). While the CHK Debt Exchange reduced the outstanding face amount of Chesapeake debt, because the new debt had a significantly higher interest rate than the old, Chesapeake's aggregate interest payments increased, putting further strain on Chesapeake's ability to pay debts when due. The CHK Debt Exchange gave rise to significant potential estate claims possibly amounting to approximately $3.8 billion. Prior to filing for bankruptcy on June 28, 2020, Chesapeake entered into a restructuring support agreement with its secured lenders whereby, amongst other things, the parties agreed to allow the potential preference claims against the

#	Company	Exchange Offer Settlement Date	Date of Subsequent Bankruptcy	Days Between Exchange Offer and Bankruptcy	Unsecured Note Recovery	Secured Debt Recovery
5	SM Energy Company[29]	6/17/2020	NA	NA	NA	NA
6	Transocean Ltd.[30]	9/11/2020	NA	NA	NA	NA

C. The Ultra Petroleum Case is a Recent Illustration of Abusive Debt Exchanges

Ultra, an exploration and production company headquartered in Englewood, Colorado, initially filed for Chapter 11 bankruptcy in April 2016. As a part of the bankruptcy proceedings, Ultra's advisor, Petrie Partners, performed a valuation of the company and rendered an opinion with an enterprise value of $5.9 billion.[31] Petrie Partners' valuation was based in part on then prevailing commodity prices and Ultra's plan to expand production. At the time, Ultra's development plan for

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secured lenders to lapse. In connection with Chesapeake's bankruptcy, the Official Committee of Unsecured Creditors objected to Chesapeake's plan of reorganization and requested standing to challenge the CHK Debt Exchange, amongst other things. After a 13-day trial, on January 16, 202, the Court confirmed Chesapeake's plan of reorganization, finding that, inter alia, although the potential claims surrounding the CHK Debt Exchange were colorable, the settlement of those claims embodied in Chesapeake's plan represented a prudent exercise of business judgment by Chesapeake's management. See Fifth Amended Plan, In re Chesapeake Energy, Case No: 20-33233 (Docket No. 2915) (Bankr. S.D. Tex. January 16, 2021).

[29]SM Energy Company Announces Expiration and Final Results of Exchange Offers and Consent Solicitations, PR Newswire (June 15, 2020) https://www.prnewswire.com/news-releases/sm-energy-company-announces-expiration-and-final-results-of-exchange-offers-and-consent-solicitations-301076585.html.

[30]Transocean Ltd. Announces Final Results Of Exchange Offers, Globe-Newswire (Sept. 9, 2020) https://www.globenewswire.com/news-release/2020/09/10/2091383/0/en/Transocean-Ltd-Announces-Final-Results-of-Exchange-Offers.html.

[31]Notice of Expert Report, In re Ultra Petroleum Resources, Case 16-32202 (Docket No. 1218-3) (Bankr. S.D. Tex. March 3, 2017).

its operations in the Pinedale and Jonah fields in Wyoming included approximately $450 million in capital expenditures in 2017, ramping up to approximately $700 million by 2018, which would equate to 10 operated rigs in 2018. In total, by 2021, Ultra expected to spend $793 million in capital expenditures. Much of the value proposition was premised on developing new wells and increasing the production of natural gas.

Ultra emerged from its 2016 bankruptcy on April 12, 2017. It had, at the time, $3.0 billion in exit financing, comprised of $400 million in secured revolving credit, an $800 million senior secured term loan, $700 million in unsecured notes due 2022, $500 million in unsecured notes due 2025, and $580 million in rights to purchase common stock of Ultra.[32]

Following its emergence, Ultra initiated a horizontal drilling program with hopes of bolstering returns from drilling. The program did not meet performance expectations and was shut down in the third quarter of 2018.[33]

At that time, natural gas prices had fallen, and the forward strip prices[34] showed no expectations of price improvement through 2022, when Ultra's revolver and 2022 notes were coming due. To cut costs of capital and operations to conserve liquidity, Ultra undertook numerous steps including borrowing additional funds under its term loan[35] and revolver[36] and selling its Uinta assets for $75 million in cash.[37]

Rating agencies, including Moody's and Standard & Poor's ("S&P"), had a consensus negative outlook on Ultra. In August 2018, Moody's downgraded Ultra's credit rating, stating that "the downgrade reflects Moody's tempered expectations for

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[32]Ultra Petroleum Emerges From Bankruptcy After Nearly a Year, HOUSTON BUS. J. (April 12, 2017) https://www.bizjournals.com/houston/news/2017/04/12/ultra-petroleum-emerges-from-bankruptcy-after.html.

[33]Ultra Petroleum Corporation, 3rd Quarter Earnings Call Transcript at 5 (Nov. 8, 2018).

[34]Strip price defined as Henry Hub natural gas.

[35]Ultra Petroleum Corporation, Quarterly Report (Form 10-Q) at 15 (Oct. 25, 2017).

[36]Ultra Petroleum Corporation, Annual Report (Form 10-K) at 4 (Feb. 28, 2019).

[37]Ultra Petroleum Corporation, Annual Report (Form 10-K) at 3 (Feb. 28, 2019).

Ultra's operational and financial performance in 2018–2019 with lower natural gas prices and production volumes."[38] In September 2018, S&P also downgraded its rating of Ultra, noting that "the downgrade reflects our assessment that Ultra is becoming increasingly vulnerable with a high debt burden that appears unsustainable over the long-term without significant improvement in operational execution and realized natural gas prices. Furthermore, although Ultra is not necessarily facing a near-term liquidity issue, it may try to facilitate a distressed exchange and could require additional relief for its leverage covenant in the next 12 to 18 months."[39]

Ultra did in fact undertake a distressed debt exchange, as S&P predicted. On October 17, 2018, Ultra announced that it had entered into an agreement in which it would exchange approximately 79.5% of its existing 2022 notes and 53.4% of its existing 2025 notes in exchange for new 9.0% cash / 2.0% PIK senior secured second lien notes due July 2024 and warrants (the "Ultra Debt Exchange").[40] The second lien notes ranked senior in right of payment to all of Ultra's then existing and future unsecured debt and were secured by second priority security interests in substantially all of Ultra's assets.[41]

Just before the announcement of the Ultra Debt Exchange, both the 2022 notes and 2025 notes were trading at distressed levels—the former at 53.9% of par and the latter at 46.6% of

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[38]Ultra Resources CFR downgraded to B2 from B1 on lower production and cash flow expectations — Moody's, Debtwire (Aug. 23, 2018).

[39]Ultra Petroleum CCR downgraded to CCC+ from B on unsustainable debt burden — S&P Debtwire (Sept. 14, 2018).

[40]Ultra Petroleum Corp Announces Exchange Agreement with Supporting Noteholder Provides Third Quarter Operations Update and Closes on Utah Asset Sale, GlobeNewswire (Oct. 17, 2018) https://www.globenewswire.com/news-release/2018/10/17/1622527/0/en/Ultra-Petroleum-Corp-Announces-Exchange-Agreement-with-Supporting-Noteholders-Provides-Third-Quarter-Operations-Update-and-Closes-on-Utah-Asset-Sale.html.

[41]Ultra Petroleum Corporation, Current Report (Form 8-K) (Dec. 21, 2018) (Indenture 9.00% Cash / 2.00% PIK Senior Secured Second Lien Notes due 2024).

par.[42] At these levels, the market obviously doubted Ultra's ability to pay its debt obligations upon maturity.

The Ultra Debt Exchange occurred over the next few months from December 21, 2018 through February 15, 2019, resulting in approximately $550 million in face value of 2022 unsecured notes and $275 million in face value of 2025 unsecured notes being exchanged, in total, for $572 million in new second-lien notes and warrants purportedly worth $10.9 million.[43]

Both Moody's and S&P again downgraded Ultra's credit rating at the time of these debt exchanges. Moody's said that it "consider[ed] Ultra's exchange . . . of debt at a significant discount to par as a distressed exchange, which is a default under Moody's definition."[44] The Ultra debt exchanges made from December 2018 through February 2019 are graphically depicted as follows:

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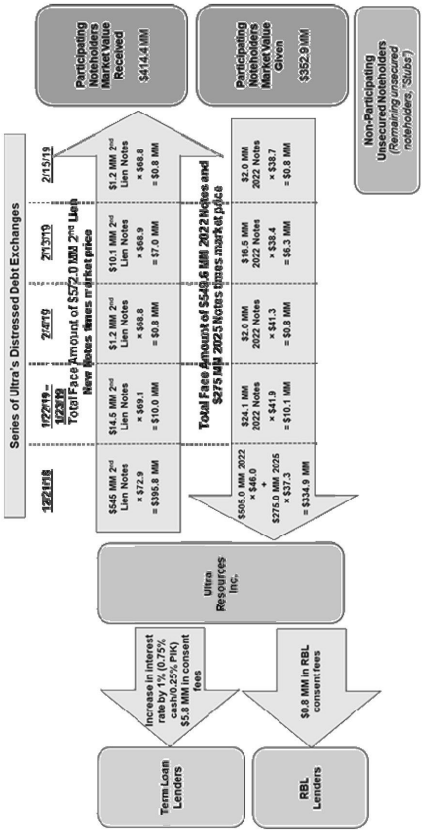
[42]Trading Price: 90400GAE1, ADVANTAGEDATA (Oct. 16, 2018); Trading Price: 90400GAA9, ADVANTAGEDATA (Oct. 16, 2018), Trading Price: 90400GAB7, ADVANTAGEDATA (Oct. 16, 2018)

[43]Ultra Petroleum Corporation, Current Report (Form 8-K) (Dec. 21, 2018); Ultra Petroleum Corporation, Current Report (Form 8-K) (Jan. 22, 2019); Ultra Petroleum Corporation, Current Report (Form 8-K) (Feb. 13, 2019); Ultra Petroleum Corporation, Annual Report (Form 10-K) (Feb. 28, 2018). The second lien notes did not have a market quote on December 21, 2018. Accordingly, this calculation uses the first day that market prices were available on January 8, 2019 as a reasonable proxy of value for the second lien notes on the first of the exchange dates, December 21, 2018.

[44]Moody's appends limited default designation to Ultra Resources' PDR MOODY'S (Dec. 21, 2018) https://www.moodys.com/research/Moodys-appends-limited-default-LD-designation-to-Pronovias-PDR—PR_440822; Ultra Petroleum Corp. Downgraded To 'SD'; Unsecured Notes Rating Lowered To 'D' STANDARD & POORS (Jan. 2, 2019).



Graph 2

Trading prices for the 2022 notes and 2025 notes following the announcement of the Ultra Debt Exchange reflected ongoing market doubt that Ultra would be able to pay the noteholders at maturity.[45] The prices at which the 2022 notes and 2025 notes were traded, from November 2018 through March 2019 are shown on Graph 3 below.

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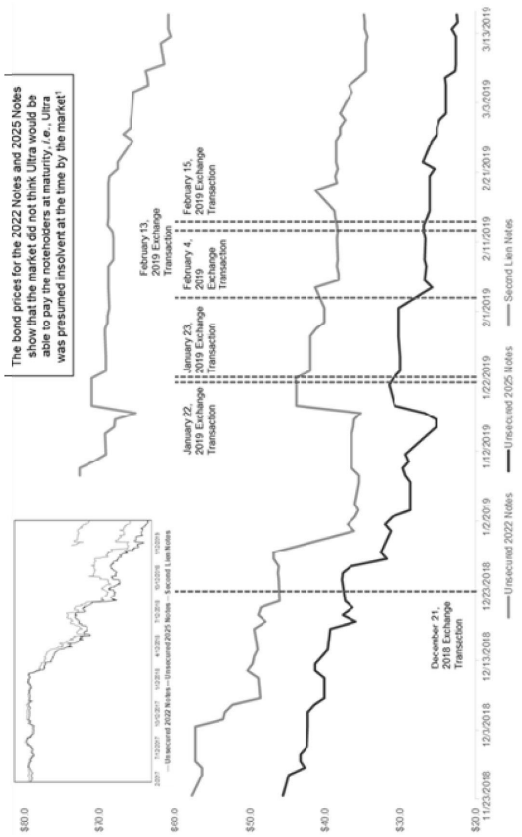
[45]Trading Price: 90400GAE1, ADVANTAGEDATA (Oct. 16-Dec. 21, 2018); Trading Price: 90400GAA9, ADVANTAGEDATA (Oct. 16-Dec. 21, 2018), Trading Price: 90400GAB7, ADVANTAGEDATA (Oct. 16-Dec. 21, 2018).



Graph 3

The Official Committee of Unsecured Creditors argued that this exchange offer was a constructive fraudulent transfer because the company was insolvent at the time and, since the trading or quoted value of the new debt issued was greater than the old debt, the company received less than reasonably equivalent value. However, the case was settled without a trial.

D. A Wave of Recent Exchange Offers

There has also been a wave of recent controversial financing transactions where distressed borrowers have accessed new capital by amending their existing secured credit agreements to permit new priority secured debt. These transactions are often open to only select existing senior lenders and disadvantage nonparticipating lenders who are subordinated as a result of the transaction. These transactions have been the subject of litigation, which in one instance has already resulted in a settlement in favor of non-participating lenders and in other instances remains pending.[46] Litigation has also been threatened with respect to the pending uptier bond exchange in Wesco Aircraft Holdings based on its insolvency.[47]

E. TriMark Lenders Conspired to Strip Covenants Prior to an Abusive Exchange Offer

TriMark USA ("TriMark"), a Centerbridge-backed company, is one of the largest providers of design services, equipment, and supplies to the foodservice industry. TriMark was one of the many companies in the foodservice industry whose financial difficulties were exacerbated by the Covid-19 pandemic.

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[46] See North Star Debt Holdings, L.P. v. Serta Simmons Bedding, LLC, No. 652243/2020 (N.Y. Sup. Ct., June 11, 2020) (dismissed without prejudice); LCM XXII LTD. v. Serta Simmons Bedding, LLC, No. 20-cv-5090 (S.D.N.Y., July 2, 2020); ICG Global Fund 1 DAC v. Boardriders, Inc., No. 655175/2020 (N.Y. Sup. Ct., Oct. 9, 2020); Audax Credit Opportunities Offshore Ltd. v. TMK Hawk Parent, Corp., No. (N.Y. Sup. Ct., Nov. 7, 2020) (settled). See also Murray Energy v. Black Diamond Commercial Finance, L.L.C, No. 19-2143 (Bankr. S.D. Ohio Ct.).

[47] Soma Biswas, Incora Recapitalization Averts Default Risk at Some Bondholders' Expense, WALL ST. J. (Mar. 31, 2022) https://www.wsj.com/articles/incora-recapitalization-averts-default-risk-at-some-bondholders-expense-11648759939.

In April 2019 S&P downgraded TriMark to CCC+, citing weakening operating performance and high leverage.[48] By June, Moody's followed suit when it downgraded TriMark to Caa1 from B3, stating that the downgrade was "largely the result of an unsustainable capital structure with excessive leverage, limited interest coverage, and negative free cash flow generation."[49]

At the time, TriMark's outstanding debt was ten times more than its EBITDA.[50] Nor was the company generating enough cash to cover the interest payments on its debt. A year later the situation proved to be worse than expected as restaurants were forced to close their doors due to the pandemic.

In hopes of addressing the company's liquidity situation, TriMark undertook an uptier exchange. On September 15, 2020, TriMark announced it had entered into an agreement in which it would issue a $120 million new money superpriority first-out term loan to a majority group of first lien term loan holders. The agreement also allowed participating first lien term loan holders to exchange, at par, their loans for new superpriority second-out term loans. The second-out loans ranked senior in right of payment to the existing first lien term loans.[51] The TriMark uptier exchange is graphically depicted in Graph 4 as follows:

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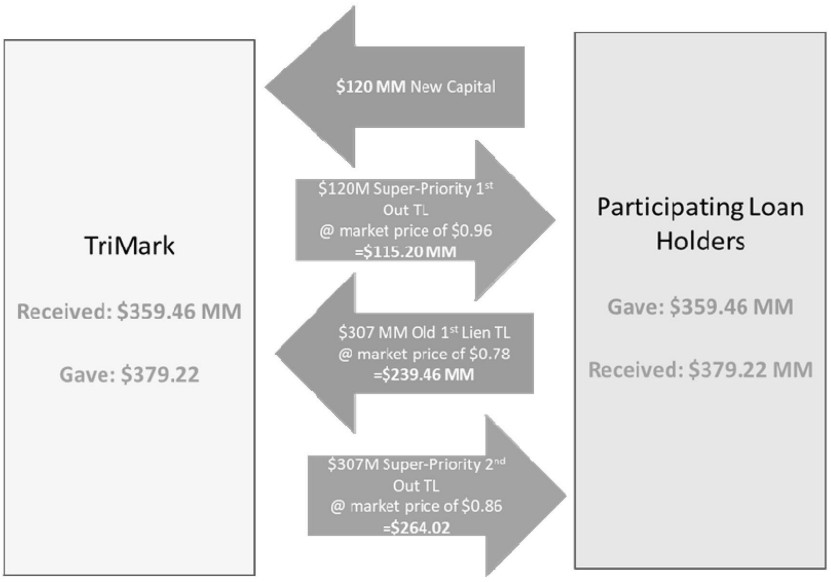
[48]TriMark credit rating downgraded to CCC+ from B on weakening operating performance —S&P, Debtwire (Apr. 30, 2019).

[49]TMK Haw Parent CFR downgraded to Caa1 from B3 on unsustainable capital structure — Moody's, Debtwire (June 7, 2019).

[50]EBITDA represents earnings before interest, taxes, depreciation, and amortization. It is a common metric used to measure the amount of cash a company generates before interest, taxes, changes in working capital, and capital expenditures.

[51]TriMark senior secured credit facilities downgraded to Ca/C from Caa2/Ca on recent recapitalization — Moody's, Debtwire (Oct. 1, 2020).

Graph 4



As set forth above, the superpriority first and second lien lenders thus jumped in front of the non-participating legacy first and second lien lenders. To accomplish this squeeze-out, a group of lenders agreed to purchase a majority of the first lien debt, and then voted to strip out its protective covenants.

Prior to the announcement, the first lien term loans were trading at 78% of par. By October 5, 2020, the loans were trading at 59% of par and would later bottom out on December 31, 2020 at 39% of par.[52]

In this instance, TriMark received approximately $359 million in value, consisting of $120 million of new capital and $239 million ($307 million at 78% of par as of the exchange date[53]) worth of existing first lien term loans. Shortly after the debt exchange, the first-out term loans were trading at 96% of par while the second-out loans were trading at 86% of par.[54] Thus, TriMark distributed approximately $379 million of value, consisting of $115 million of first-out term loans ($120 million at 96% of par) and $264 million of second-out term loans ($307 million at 86% of par), and received approximately $20 million less. Therefore, TriMark did not receive reasonably equivalent value through this debt exchange. Additionally, the price of the first lien term loan immediately following the debt exchange indicates that the market believed TriMark to be insolvent.

In addition, those unable to participate in the exchange were severely harmed as the first lien credit agreement was amended to strip out substantially all of the existing covenants and the non-participating loans fell from 78 cents to 59 cents after the transaction and 39 cents by December.[55]

Litigation ensued in January 2022, and a settlement gave the non-participating first lien lenders the right to swap out their loans on a dollar-for-dollar basis for the second-out term loan, which was junior to the first-out term loan. Because TriMark did not receive reasonably equivalent value, and

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[52]Trading Price: 02337NAB5, Bloomberg L.P. (Dec. 31, 2020).

[53]Trading Price: 02337NAB5, Bloomberg L.P. (Dec. 31, 2020).

[54]TriMark Minority TL Lenders Organize With Selendy & Gay as Legal Advisor, Evaluating Options Including Litigation, Reorg (Sept. 30, 2020).

[55]TriMark Minority Lenders Plan to Litigate Non-Pro-Rate Recapitalization in Coming Weeks, Reorg (Oct. 9, 2020).

market prices indicated that TriMark would not be able to meet its debt obligations as they came due, TriMark was a good candidate for avoidance of the transfer as a constructive fraudulent transaction, but this argument does not appear to have been asserted by plaintiffs.

F. The Serta Simmons Transaction Raises Concerns

Serta Simmons ("Serta") is one of the largest bedding manufacturers in North America. The company has struggled in recent years amid, inter alia, increased imports and online competition. The forced closure of retail stores due to the pandemic worsened Serta's situation, prompting the company to seek a liability-management transaction.[56]

On June 8, 2020, Serta announced that it had entered into a transaction support agreement with the majority of its first lien and second lien term loan holders. The deal included $200 million of new superpriority first-out debt and an exchange of certain existing first lien and second lien term loans for $875 million of super-priority second-out debt. The superpriority first-out and second-out debt would be senior to the existing first and second lien term loans. The participating first liens would receive $74 of the super-priority "second out" debt per $100 of existing loans while the second liens would receive $39 of super-priority "second out" debt per $100 of existing loans.[57]

At the time of the exchange, the first lien term loans were quoted at 25 cents on the dollar and the second lien term loans were quoted at 15 cents—a clear indication that the market believed Serta to be insolvent.[58] The Serta exchange transaction is graphically depicted in Graph 5 as follows:

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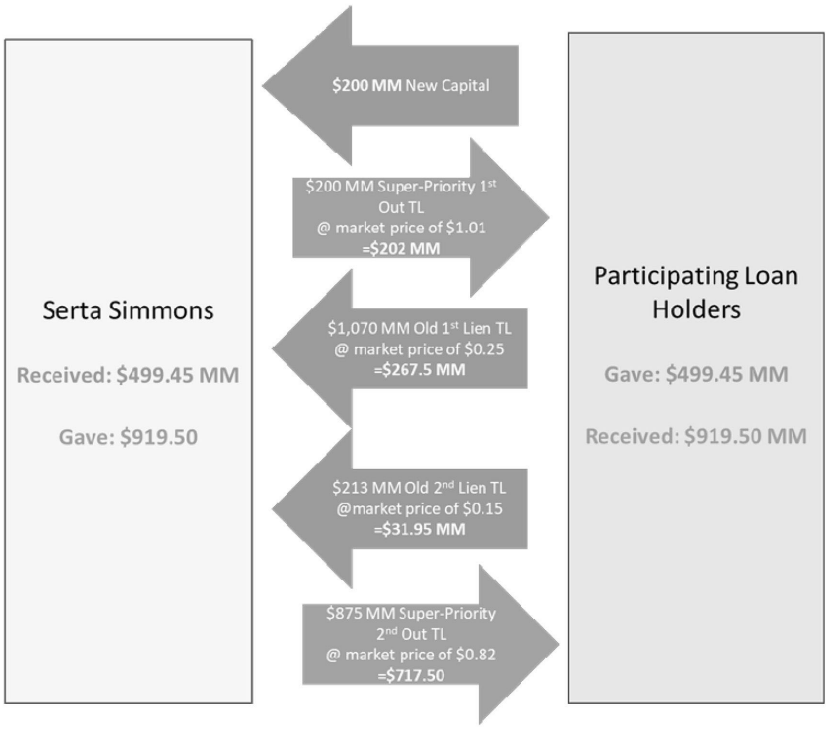
[56]Matt Wirz, Apollo Sues Serta Simmons and Owner Advent Over Debt Dispute, WALL ST. J. (June 11, 2020) https://www.wsj.com/articles/apollo-sues-serta-simmons-and-owner-advent-over-debt-dispute-11591906294.

[57]Serta Simmons Enters Into Agreement with Majority of 1L, 2L Lenders to Reduce Net Debt by $400M, Provide $200M New Money Super-Priority Debt, REORG (June 8, 2020) https://app.reorg.com/v3#/items/intel/5881?item_id=106877.

[58]Trading Price: 81753HAB7, BLOOMBERG L.P. (June 22, 2020) Trading Price: 81753HAD3, BLOOMBERG L.P. (June 22, 2020).

A Market Based Theory to Demonstrate Lack of Reasonably Equivalent Value for Abusive Debt Exchange Offers

Graph 5



Under these circumstances and given that $1.07 billion principal amount of first lien term loans and $213 million principal amount of second lien term loans were exchanged, Serta received approximately $267.5 million ($1.07 billion at 25% par) worth of first lien loans and $32 million ($213 million at 15% par) worth of second lien loans for a total of $299.45 million in exchanging term loans. When considering the $200 million of new capital provided, the total value Serta received is approximately $499.45 million.

When Serta's new "superpriority second-out" debt began trading, it was priced at 82 cents.[59] As a result, the market value of the "superpriority second-out debt" was approximately $717.5 million ($875 million principal amount at 82%), a considerable amount more than the $299.5 million of value the company received via its exchanged first and second lien term loans. In addition, the "superpriority first-out" loans soon traded at around 101 cents, giving "the first-out" loans a market value of $202 million ($200 million at 101% of par).[60] In aggregate, Serta gave out approximately $919.5 million of value while only receiving approximately $499.5 million. The historical debt prices for Serta's existing first lien debt before and after the exchange, and for its "superpriority first-out" debt and "superpriority second-out" debt after the exchange, are shown on Graph 6 below.

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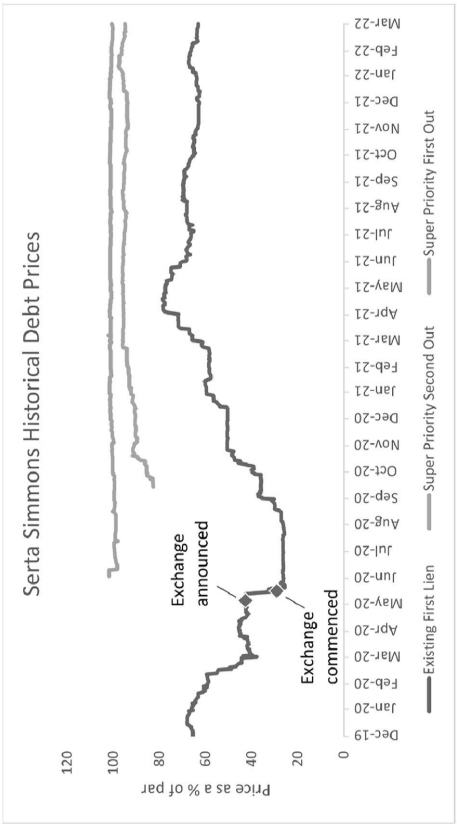
[59]Trading Price: 81753HAG6, BLOOMBERG L.P. (Oct. 13, 2020).

[60]Trading Price: 81753HAF8, BLOOMBERG L.P. (July 2, 2020).



Graph 6

Accordingly, this situation may qualify as a constructive fraudulent transfer as market prices indicated that Serta was insolvent at the time of the exchange and the company did not receive reasonably equivalent value from the transaction. While litigation remains ongoing and the transaction is being challenged on other grounds,[61] the preceding constructive fraudulent theory has yet to be raised.

II. Determining Reasonably Equivalent Value

Regardless of the vehicle chosen for the litigation, value is viewed the same way.[62] However, neither the Uniform Act[63] nor the Bankruptcy Code[64] sets forth all the contours of "value," much less "reasonably equivalent value."[65] Case law has established a broad scope to "value," including "any bene-

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[61] Faegre Drinker currently represents a lender who was left out of Serta's uptier exchange.

[62] *In re Reisner*, 357 B.R. 206, 216 (Bankr. E.D. N.Y. 2006) ("[t]he analysis under Florida law of whether reasonably equivalent value was given is identical to that under Section 548 of the Bankruptcy Code"); *In re Solomon*, 300 B.R. 57, 63 (Bankr. N.D. Okla. 2003), order aff'd, 299 B.R. 626 (B.A.P. 10th Cir. 2003) ("Many courts, considering the similarities in purpose and language, have concluded that the UFTA and § 548 are in pari materia and that the same analysis applies under both laws."); *In re Spatz*, 222 B.R. 157, 164 (N.D. Ill. 1998) ("Because the provisions of the UFTA parallel § 548 of the Bankruptcy Code, findings made under the Bankruptcy Code are applicable to actions under the UFTA").

[63] "Value is given for a transfer or an obligation if, in exchange for the transfer or obligations, property is transferred or an antecedent debt is secured or satisfied, but value does not include an unperformed promise made otherwise than in the ordinary course of the promisor's business to furnish support to the debtor or another person." UVTA § 3(a).

[64] Jack F. Williams Valuation Tenets in Bankruptcy, AM. BANKR. INST. J. 32 (Nov. 2001) (arguing that the general definition of value under the Bankruptcy Code is found in § 506(a), which provides that "[s]uch value shall be determined in light of the purpose of the valuation and of the proposed disposition or use of such property . . ." and that § 548(d)(2) defines value as "property, or satisfaction or securing of a present or antecedent debt of the debtor"); c.f. Jordi Guso & Paul A. Avron Defining Value in 11 U.S.C. 363(f)(3) Is Face Amount of the Claim Secured by the Lien or the Economic Value of the Lien AM. BANKR. INST. J. 36 (Nov. 2004).

[65] *BFP v. Resolution Trust Corp.*, 511 U.S. 531, 535, 114 S. Ct. 1757, 128 L. Ed. 2d 556, 25 Bankr. Ct. Dec. (CRR) 1051, 30 Collier Bankr. Cas. 2d (MB) 345, Bankr. L. Rep. (CCH) P 75885 (1994) ("Of the three critical terms 'reasonably equivalent value,' only the last is defined: 'value' means, for

fit" to the debtor, "direct or indirect" and "any kind of enforceable executory promise."[66] As a result, courts have slowly chipped away at the marble to determine a workable framework of value and whether the amount given is reasonably equivalent to the amount received.

A. ***Totality of the Circumstances:***

Whether a debtor received "reasonably equivalent value" in a transfer is ordinarily a question of fact.[67] Almost all Circuit Courts of Appeal, therefore, answer this question by considering the totality of the circumstances to determine whether the "value" received was reasonably equivalent to the value transferred.[68] Some courts' consideration of the totality of the circumstances is limited to certain questions.[69] If the debtor gained at least some value, then the court will compare whether the debtor got roughly the value that it gave. In doing so, courts of appeal generally look at (1) the "fair market value" of the benefit received as a result of the transfer, (2) "the existence of an arm's-length relationship between the debtor and the transferee," and (3) the transferee's good

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purposes of § 548, 'property, or satisfaction or securing of a . . . debt of the debtor,' ").

[66] 5 Collier on Bankruptcy ¶ 548.03 (16th 2021); see *Rubin v. Manufacturers Hanover Trust Co.*, 661 F.2d 979, 991–92, 8 Bankr. Ct. Dec. (CRR) 297 (2d Cir. 1981) (establishing the "indirect benefit" rule).

[67] *In re Dewey & LeBoeuf LLP*, 518 B.R. 766, 785–85, 60 Bankr. Ct. Dec. (CRR) 80 (Bankr. S.D. N.Y. 2014).

[68] See *Barber v. Golden Seed Co., Inc.*, 129 F.3d 382, 387 (7th Cir. 1997); *Matter of Dunham*, 110 F.3d 286, 289, 37 Collier Bankr. Cas. 2d (MB) 1307, Bankr. L. Rep. (CCH) P 77413 (5th Cir. 1997); *In re R.M.L., Inc.*, 92 F.3d 139, 148–149, 29 Bankr. Ct. Dec. (CRR) 591, 36 Collier Bankr. Cas. 2d (MB) 498 (3d Cir. 1996); *Matter of Besing*, 981 F.2d 1488, 1495 n.14, 23 Bankr. Ct. Dec. (CRR) 1590, Bankr. L. Rep. (CCH) P 75156 (5th Cir. 1993); *In re Morris Communications NC, Inc.*, 914 F.2d 458, 467–68, 23 Collier Bankr. Cas. 2d (MB) 1456, Bankr. L. Rep. (CCH) P 73621 (4th Cir. 1990); *In re Ozark Restaurant Equipment Co., Inc.*, 850 F.2d 342, 344–345, 17 Bankr. Ct. Dec. (CRR) 1321, 19 Collier Bankr. Cas. 2d (MB) 35, Bankr. L. Rep. (CCH) P 72344 (8th Cir. 1988); see also 5 Collier on Bankruptcy ¶ 548.05 (16th 2020).

[69] *In re Fruehauf Trailer Corp.*, 444 F.3d 203, 212–13, 46 Bankr. Ct. Dec. (CRR) 100, 37 Employee Benefits Cas. (BNA) 1796, Bankr. L. Rep. (CCH) P 80483 (3d Cir. 2006).

faith.[70] Other considerations include the difference between the amount transferred and the fair market value, and the percentage of the fair market value that was paid[71] Determining the "fair market value" can be relatively easy depending on the source of the value and the market. If it is property (which includes cash and the payment of money[72]), valuation should be simple: how much can the asset be sold for or what number is on the note.[73] When valuing a company, a recognized source of value is stock price and market capitalization.[74] If the source of value is an indirect benefit or is intangible, valuation is more difficult.[75] Overall, courts must examine the entire situation, even multistep transactions.[76]

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[70]Mellon Bank, 92 F.3d at 149–49, 153; *In re TSIC, Inc.*, 428 B.R. 103, 113 (Bankr. D. Del. 2010).

[71]Cooper, 914 F.2d at 467; see also *In re Washington*, 232 B.R. 340, 342 (Bankr. E.D. Va. 1999) (citation omitted); *BFP v. Resolution Trust Corp.*, 511 U.S. 531, 548, 114 S. Ct. 1757, 128 L. Ed. 2d 556, 25 Bankr. Ct. Dec. (CRR) 1051, 30 Collier Bankr. Cas. 2d (MB) 345, Bankr. L. Rep. (CCH) P 75885 (1994) (holding that an asset's price at a foreclosure sale is, as a matter of law, its "reasonably equivalent value," but limiting this holding to foreclosure sales).

[72]*In re Lindell*, 334 B.R. 249, 255, 45 Bankr. Ct. Dec. (CRR) 108, 54 Collier Bankr. Cas. 2d (MB) 1853 (Bankr. D. Minn. 2005).

[73]Lindell, 334 B.R. at 255 (after an expert witness valued promissory notes at $130,000 based on face value, interest rate, and collateral, court found that $50,000 in cash was not reasonably equivalent value).

[74]See *VFB LLC v. Campbell Soup Co.*, 482 F.3d 624, 631, 48 Bankr. Ct. Dec. (CRR) 3 (3d Cir. 2007) (looking to a corporation's stock price after a purchase to determine whether it paid reasonably equivalent value for its new assets, despite acknowledging fraudulent public disclosures). In *Campbell*, a subsidiary purchased many of its parent's assets for $500 million and had a market capitalization of $1.1 billion for 10 months after the transfer, before eventually filing for bankruptcy. The Bankruptcy Court, and subsequently the Third Circuit, held that a stock price was a valid measurement of value despite also finding that the share price was initially inflated by misleading public disclosures. Since the subsidiary paid $500 million and subsequently had a market capitalization of $1.1 billion, it gained more than reasonably equivalent value.

[75]*In re R.M.L., Inc.*, 92 F.3d 139, 148, 29 Bankr. Ct. Dec. (CRR) 591, 36 Collier Bankr. Cas. 2d (MB) 498 (3d Cir. 1996) (valuing a commitment letter and citing other examples of court efforts to value intangibles); *In re Green*, 268 B.R. 628, 651 (Bankr. M.D. Fla. 2001) (debtors "understandably felt a moral or family obligation" to pay for their daughter's wedding or to

B. *Valuing the Old Debt in a Debt Exchange*

Both the Bankruptcy Code and Uniform Act state that "value" includes the satisfaction or securing of a present or antecedent debt of the debtor.[77] The Bankruptcy Code and the Uniform Act, however, leave courts to answer how to evaluate the satisfaction of that debt. Courts have regularly held that if the transfer amounts to a "dollar-for-dollar" reduction in debt, the debtor has received reasonably equivalent value.[78] In the situation where the debtor pays $100 to satisfy a debt

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make a sizeable wedding gift but satisfying such a moral obligation is not reasonably equivalent value, nor is "love and affection").

[76]See, e.g., Lindell, 334 B.R. at 255 ("a court must examine the entire situation"); *In re Tribune Company Fraudulent Conveyance Litigation*, 10 F.4th 147, 164 (2d Cir. 2021), cert. denied, 142 S. Ct. 1128, 212 L. Ed. 2d 18 (2022), (citing *In re Sabine Oil & Gas Corporation*, 547 B.R. 503, 541 (Bankr. S.D. N.Y. 2016), stay pending appeal denied, 548 B.R. 674, 62 Bankr. Ct. Dec. (CRR) 138 (Bankr. S.D. N.Y. 2016) and aff'd, 562 B.R. 211 (S.D. N.Y. 2016)) (collapsing multiple transactions as one cohesive fraudulent transfer).

[77]11 U.S.C.A. § 548(d)(2); UVTA § 3(a), cmt. 2 ("Section 3(a) is adapted from Bankruptcy Code § 548(d)(2)(A) (1984) . . . The definition in Section 3 is not exclusive. "Value" is to be determined in light of the purpose of the Act to protect a debtor's estate from being depleted to the prejudice of the debtor's unsecured creditors. Consideration having no utility from a creditor's viewpoint does not satisfy the statutory definition. The definition does not specify all the kinds of consideration that do not constitute value for the purposes of this Act—e.g., love and affection.").

[78]5 Collier on Bankruptcy ¶ 548.03 (16th 2022); see, e.g., *Matter of Louisiana Pellets, Inc.*, 838 Fed. Appx. 45, 50 (5th Cir. 2020) (per curiam) (unpublished and not precedential, pursuant to 5th Cir. R. 47.5) ("When a debtor makes a payment on antecedent debt and receives a dollar-for-dollar reduction of that debt, however, the question is easy because the debtor by definition receives reasonably equivalent value—indeed, exactly equivalent value, assuming, of course that the debt itself was based upon value"); *In re Southeast Waffles, LLC*, 702 F.3d 850, 857, 57 Bankr. Ct. Dec. (CRR) 80, Bankr. L. Rep. (CCH) P 82389, 2012-2 U.S. Tax Cas. (CCH) P 50708, 110 A.F.T.R.2d 2012-6953 (6th Cir. 2012) ("Typically, a dollar-for-dollar reduction in debt constitutes—as a matter of law—reasonably equivalent value for purposes of the fraudulent-transfer statutes"); *Freeland v. Enodis Corp.*, 540 F.3d 721, 735, 50 Bankr. Ct. Dec. (CRR) 134, 60 Collier Bankr. Cas. 2d (MB) 524, Bankr. L. Rep. (CCH) P 81315 (7th Cir. 2008) ("payment of the accrued interest constituted 'dollar-for-dollar forgiveness of a contractual debt,' which is 'reasonably equivalent value.' "); *In re Licking River Mining, LLC*, 603 B.R. 336, 366 (Bankr. E.D. Ky. 2019), as amended, (July 19, 2019); *In re Propex, Inc.*, 415 B.R. 321, 324 (Bankr. E.D. Tenn. 2009) (finding that a $20 million payment pursuant to an amended credit agreement was made

that everyone agrees is worth $100, then necessarily the debtor has received reasonably equivalent value. This accords with the statute and common sense.

Courts have not effectively grappled with the issue of what "dollars" need to be matched when the face value of the debt differs from the trading value as reflected on a recognized market. Case law on "dollar-for-dollar" reduction of debt has not adequately confronted the possibility that debt can be not only be traded and valued, especially when the debtor is a large company, but also can be purchased and extinguished by the debtor for substantially less than face value.[79]

When a company's debt is trading at a discount and it faces insolvency, the economic benefit received by the debtor and its creditors by repaying this debt out of bankruptcy is likely to be less than the face value of this debt.[80] That is because

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for "reasonably equivalent value" as a matter of law because the payment reduced the principal balance of the indebtedness dollar-for-dollar.).

[79] One court came close: *ASARCO LLC v. Americas Mining Corp.*, 396 B.R. 278 (S.D. Tex. 2008). In ASARCO, a debtor-in-possession (ASARCO) and its subsidiary sued their parent and parent's parent for constructive fraud after the subsidiary transferred certain stock holdings to the parent in exchange for $765 million, of which $50 million in cash was earmarked to pay off bonds at par value. ASARCO, 396 B.R. at 339. At the time, however, the outstanding bonds were trading below par value. ASARCO argued that "because it was required to use the $50 million to pay off bonds above their market trade value, it did not receive the full value of the $50 million" that it received for the stock transfer. ASARCO, 396 B.R. at 340. The court, without further explanation, held that the bonds' discount did not in turn discount the value of the $50 million received because "[e]ven if ASARCO purchased the bonds off the market for 50 cents on the dollar, it would have had to use $ 50 million to do so." ASARCO, 396 B.R. at 340. Although insightful, ASARCO's fact pattern is distinguishable from an uptier exchange because the challenged transaction was not the bond repayment but the receipt of cash for a stock transfer. Thus, while at least one court has recognized that bonds may trade below face value, it did not consider the possibility that a debtor may choose to extinguish debts for less than face value or how that might interact with the idea of "dollar-for-dollar" repayment.

[80] "Debt-for-debt exchanges are often at a significant discount. . .from the face amount of debt. . .Just above the trading value of your debt is a good target price. At least that is where discussions should start if you are in fact going to pursue some type of debt buyout or debt exchange." See OnAir with Akin Gump, Managing the New Reality: Opportunities & Landmines for Energy Companies Right Now, AKIN GUMP STRAUSS HAUER & FELD LLP (April 6, 2020) https://www.akingump.com/en/news-insights/podc

the recovery on an allowed unsecured claim in bankruptcy, except in rare cases, will be substantially less than the face amount of the debt.[81] In other words, as some bankruptcy professionals say, after filing a petition for bankruptcy, the debt will be repaid in "bankruptcy dollars," which will almost always be worth less than "real dollars" to take into account the haircut being applied to the applicable class of creditors.[82]

Moreover, the face amount of a credit instrument does not necessarily correlate with its value, as reflected by market prices.[83] Thus, when engaging in totality of the circumstances and net effect analyses of an exchange for reasonably equivalent value purposes, courts should shift their focus to the market trading prices of the instruments at issue, rather than their face values.[84] That shift in focus acknowledges the disconnect between face amount of indebtedness and value, and accounts for two fundamental principles in finance—namely, the time value of money and the relationship between risk and return. All other things being equal, a rational investor will generally prefer to receive the same amount of value sooner, rather than later.[85] And, all other things being equal,

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ast/managing-the-new-reality-opportunities-and-landmines-for-energy-companies-right-now.html (recorded and transcribed on March 12, 2020).

[81] See *Matter of Mobile Steel Co.*, 563 F.2d 692, 700, 15 C.B.C. 1 (5th Cir. 1977) ("the assertion of a claim in bankruptcy is, of course, not an attempt to recover a judgment against the debtor but to obtain a distributive share in the immediate assets of the proceeding.").

[82] Emil A. Kleinhaus & Alexander B. Lees, Debt Repayments as Fraudulent Transfers 8 Am. Bankr. L. J. 307, 322 (2014) ("If a debtor has assets sufficient to pay only a fraction of its unsecured obligations and repays an unsecured debt in full, the claim satisfied by the debtor has a value in bankruptcy (and in the marketplace) that is lower than its face amount. In that circumstance, one could argue that the economic benefit received by the debtor by repaying its debt is less than, rather than equal to, the face value of the debt.").

[83] Stephen G. Kellison, The Theory of Interest, 209 (2d ed. 1991); Edward I. Altman, Bankruptcy, Credit Risk, and High Yield Junk Bonds 153 (2002).

[84] C.f. Campbell, 482 F.3d at 629–30 ("Even if, as [the plaintiff] implies, the market was suffering from some irrational exuberance in establishing [the debtor's] stock price, that gives me no basis for second-guessing the value that was fairly established in open and informed trading.") (quoting the lower court's opinion, 2005 WL 2334606 at *26) (internal quotation marks omitted).

[85] Bruce Tuckman, Fixed Income Securities, 3-4 (1st ed. 1996).

the creditworthiness of a counterparty is a key aspect of ascribing value to its debts.[86] Efficient credit market pricing will automatically factor in the time value of money and the creditworthiness of the obligor, making it the "best evidence of value" of the debt instruments being exchanged.[87] Value is viewed objectively, and the underlying question is whether the consideration received by the debtor matches the value that it gave.[88]

III. For Fair Market Value Exchanges, Where Recovery Is Less Than Face, Courts Should Use the Totality of the Circumstances to Assess Reasonably Equivalent Value.

As noted above, courts should consider the totality of the circumstances in assessing whether a debtor received reasonably equivalent value. While, with respect to a debt exchange, the case law has yet to be developed, we can envision the following factors being relevant:

- Market value of the Old Debt redeemed, which in an efficient market reflects the time value of money and probability of payment default;[89]
- Ability of the debtor to purchase its debt in the market;
- Original maturity of the Old Debt and perhaps other rights of the holders as it impacts the ability to leverage the debtor in the near term;
- Value of New Debt provided in the debt exchange, which involves the exchange ratio for the underlying debt

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[86] KELLISON, supra note 82 at 214

[87] SHANNON P. PRATT & ROGER J. GRABOWSKI, COST OF CAPITAL, 7, 62–68 (4th ed. 2010). ALTMAN, supra note 82 at 153. Robert J. Stark, Jack. F. Williams, & Anders J. Maxwell, Market Evidence, Expert Opinion, and the Adjudicated Value of Distressed Business, BUS. LAW., Vol. 68 (August 2013).

[88] Wilkinson, 196 F. App'x at 342 (indirect benefits must be "concrete and quantifiable"); *In re Canyon Systems Corp.*, 343 B.R. 615, 640 (Bankr. S.D. Ohio 2006) ("The cases have emphasized that 'value' must be viewed from an objective standpoint").

[89] There are instances when market value may not reflect a firm's intrinsic value due to (i) access to liquidity, (ii) inefficient market; or (iii) lack of availability of information. Thus, it is important to compare a fundamental valuation analysis to determine if market trading prices are representative of a firm's fair market value.

exchange and the value the market ascribes to the New Debt after the exchange;

- Trading prices of non-participating remaining Old Debt after confirmation of an exchange, which can reflect improvement or impairment of market perception of repayment; and
- Solvency of the debtor immediately before and after the exchange, which can provide insights into value received by the company in improving its credit profile.

As to this list, we think market value is far and away the most important factor. That said, in the right situation, other factors may prove relevant. Of critical importance, courts should thoughtfully consider the various issues in developing case law in this space.

A comprehensive article by Emil Kleinhaus and Alexander Lees, *Debt Repayments as Fraudulent Transfers*, describes the theory espoused in this article that a below market exchange can be attacked as a constructive fraudulent transfer:

> when projected future recoveries on the satisfied claim are taken into account, the quotient of value received by the debtor is open to question. If the debtor is solvent or the debt at issue is fully secured, then the debtor receives a dollar of benefit for every dollar repaid. On the other hand, if a debtor has assets sufficient to pay only a fraction of its unsecured obligations and repays an unsecured debt in full, the claim satisfied by the debtor has a value in bankruptcy (and in the marketplace) that is lower than its face value. In that circumstance, one could argue that the economic benefit received by the debtor by repaying its debt is less than, rather than equal to, the face value of the debt.[90]

Although this argument has some force, the Kleinhaus article warns:

> there are still sound reasons to treat the repayment of an unsecured debt as providing value equal to its face amount, even when the debtor is insolvent. If debt repayments could be attacked as constructively fraudulent on the basis that an insolvent's debts are worth less than their face amount, essentially all pre-bankruptcy debt repayments could be set aside as constructive fraudulent transfers. In that case, Congress's comprehensive scheme for preference avoidance under section 547 of the Bankruptcy Code—including the numerous defenses

[90] Kleinhaus & Lees, supra note 82 at 322.

> to preference claims, as well as the strict time limitations placed on such claims— could be bypassed.[91]

In the first instance, we do not agree with the Kleinhaus proposition that "essentially all pre-bankruptcy debt repayments could be set aside as constructive fraudulent transfers." Rather, a court would evaluate a given debt exchange under the totality of the circumstances. If, for example, a debtor issued the same face amount of New Debt in exchange for Old Debt trading at 90 cents on the dollar, a court might well conclude that, even though there was not a dollar-for-dollar matching, the debtor received reasonably equivalent value upon consideration of all the circumstances. By contrast, however, if a debtor issued New Debt in exchange for Old Debt trading at 20 cents on the dollar—and indeed passed on the opportunity to buy that Old Debt on the open market for the discounted price—common sense tells us that there is a fraudulent transfer afoot.

Regarding the concern about the preference avoidance scheme, the case law around avoiding preferential repayment of debts does provide insight into how repaying a group of favored lenders may be perceived by courts. But suggesting that avoiding undervalued debts as constructive fraud will unravel the Bankruptcy Code's preference scheme goes too far.

Although a thorough discussion of the "actual fraud" avenue for challenging an uptier exchange is beyond the scope of this article, the debtor's intent in making the transaction deserves discussion. While a plaintiff may struggle to prove that the debtor exchanged debt with the intent to "hinder, delay, or defraud" creditors,[92] it would be relatively easy to prove that the debtor, at the very least, intended to prefer certain creditors over others. After all, uptier exchanges involve transactions made available to only a select group,

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[91] Kleinhaus & Lees, supra note 82 at 322.

[92] But see ASARCO 396 B.R. at 386–87 (S.D. Tex. 2008) ("a transfer may be made with fraudulent intent even though the debtor did not intend to harm creditors but knew that by entering the transaction, creditors would inevitably be hindered, delayed, or defrauded").

resulting in superpriority status for the favored lenders and subordinated status for the disfavored lenders.[93]

For years, courts wrestled with the question of whether the intent to prefer creditors made a transfer actionable as a fraudulent transfer. As the Supreme Court noted in 1913, bankruptcy law "recognizes the difference between the intent to defraud and the intent to prefer, and also the difference between a fraudulent and a preferential conveyance."[94] The intent to prefer a creditor, according to the Court, is *malum prohibitum*, "innocent and valid . . .unless made within the prohibited period," but in order for a transfer to be actionable as a fraudulent transfer, the debtor's act must be *malum per se*, "inherently and always vicious."[95] Since then, a principle has pervaded case law that "mere intent to prefer one creditor over another, by using scarce resources to satisfy one obligation rather than a competing obligation, is *not* sufficient to establish the intent to hinder, delay, or defraud creditors."[96]

Under this principle, any uptier exchange could potentially be immune from allegations of actual fraud. Courts following this principle have held, rather explicitly, that repayment of debt is a preference and not a fraudulent transfer, regardless of ulterior motives.[97] If an uptier exchange is most easily compared to a repayment of debt (the debtor repays old liens with superpriority liens), and repayment of debt amounts to a preference, an uptier exchange can never have the requisite intent to be an actual fraudulent transfer.

Recently, however, courts have moved away from the strict dichotomy between preferences and actual fraud. Now, debt

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[93] *Richardson v. Germania Bank of City of New York*, 263 F. 320, 322 (C.C.A. 2d Cir. 1919) ("[o]ne cannot wish to favor some creditors, without also wishing (perhaps regretfully) to treat others with disfavor.").

[94] *Van Iderstine v. National Discount Co.*, 227 U.S. 575, 582, 33 S. Ct. 343, 57 L. Ed. 652 (1913).

[95] Van Iderstine, 227 U.S. at 582.

[96] Kleinhaus & Lees, supra note 82, at 338.

[97] See *Boston Trading Group, Inc. v. Burnazos*, 835 F.2d 1504, 1509 (1st Cir. 1987) (Breyer, J.) (the object of fraudulent conveyance law is "to see that the debtor uses his limited assets to satisfy *some* of his creditors" and therefore does not extend to repayment of valid debts); *B.E.L.T., Inc. v. Wachovia Corp.*, 403 F.3d 474, 477 (7th Cir. 2005) (repayment of debt by a debtor engaged in fraud was not an actual fraudulent transfer because "in the end this is nothing but a preference."

repayments have been avoided as actual fraudulent transfers in situations in which repayments of debts are themselves an integral part of a scheme to benefit the debtor and its shareholders at the expense of creditors who should have priority to the debtor's value.[98] Ponzi schemes dominate the case law in this area.[99] Ponzi scheme payments are arguably transactions to repay an antecedent debt: the principal initially invested.[100] However, courts have held that payment recipients can avoid liability for the underlying fraud only by proving their good faith under § 548(c); mere repayment on an antecedent debt is not enough.[101]

In summary, the doctrine that "intent to prefer—i.e., knowledge that a debt repayment will permit one creditor to recover more than others—is fundamentally distinct from an intent to hinder, delay, or defraud creditors" has generally been upheld.[102] In some situations—Ponzi schemes—debt repayments have been avoided as actual fraud because they were integral to broader schemes that, through the use of preferential transfers, were designed to enrich the debtor at the expense of creditors.[103] We believe that courts can—and under the more modern view do—make appropriate distinctions concerning the legal analysis as between preferential

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[98]Kleinhaus & Lees, supra note 82.

[99]See, e.g., *Picard v. Katz*, 462 B.R. 447, 55 Bankr. Ct. Dec. (CRR) 133, Bankr. L. Rep. (CCH) P 82077 (S.D. N.Y. 2011) (abrogated by, Securities Investor Protection Corp. v. Bernard L. Madoff Inv. Securities LLC, 513 B.R. 437, 59 Bankr. Ct. Dec. (CRR) 188 (S.D. N.Y. 2014)) (trustee of Bernard Madoff's brokerage firm sought return of Ponzi-scheme payments to the owners of the New York Mets); *In re Dreier LLP*, 452 B.R. 391 (Bankr. S.D. N.Y. 2011) (dismissing constructive fraud claims and agreeing with *Picard* that actual fraud claims could be defeated only by a demonstration of good faith).

[100]See Kleinhaus & Lees, supra note 82 at 336 (discussing *Picard*).

[101]Picard, 462 B.R. at 545.

[102]Kleinhaus & Lees, supra note 82 at 340–41.

[103]Kleinhaus & Lees, supra note 82 at 340–41 ("By contrast, debt repayments are *not* avoidable as fraudulent transfers based on their incidental effect on recoveries of non-preferred creditors; if they were, fraudulent transfer law would infringe upon the statutory scheme enacted to address preferences").

and fraudulent transfer claims. Thus, concerns about obviating the preference scheme have less force in our view.[104]

IV. Conclusion

At the end of the day courts try to determine what effect the transaction had on the net health of the debtor. Generally, the concept of reasonably equivalent value protects creditors from depleting the value available in the estate.[105] As such, the net effect of the exchange on the financial health of the issuer may be critical in determining reasonably equivalent value.[106] A focus on the financial health necessarily involves

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[104]This dichotomy between preferences and fraudulent transfers has also been considered in the context of constructive fraud, typically as an inquiry into "bad faith." See, e.g., *In re Sharp Intern. Corp.*, 403 F.3d 43, 54, 44 Bankr. Ct. Dec. (CRR) 146 (2d Cir. 2005) ("the decisive principle in this case is that a mere preference between creditors does not constitute bad faith"). The Uniform Fraudulent Conveyance Act ("UFCA"), the precursor to the UFTA and UVTA, included the transferee's good faith as an element of "fair consideration," the precursor to "reasonably equivalent value." UVTA § 4 cmt.3. The same was true of New York's Debtor-Creditor Law, only recently replaced by the UVTA in 2020. Kleinhaus & Lees, supra note 82 at 319; compare NY Debt & Cred L. §§ 270 to 81 (2019) with NY Debt. & Cred. L. §§ 270-81-A; see also Uniform Voidable Transactions Act Adopted in New York, Jones Day — Insights (Apr. 2020) https://www.jonesday.com/en/insights/2020/04/uniform-voidable-transactions-act-adopted-in-new-y. Under the UFCA and New York law, the Second Circuit held that the requirement for "good faith" was meant to stop *insider* payments, but does not otherwise invite inquiry into a non-insider creditor's state of mind, unless the creditor participated in the alleged misconduct. Kleinhaus & Lees, supra note 82 at 321. Thus, "preferential repayment of pre-existing debts to some creditors does not constitute a fraudulent conveyance, whether or not it prejudices other creditors," unless the creditor-transferee has "actual intent . . . to hinder, delay, or defraud either present or future creditors," at which time an allegation for actual fraud is merited. See *HBE Leasing Corp. v. Frank*, 48 F.3d 623, 634, 31 Fed. R. Serv. 3d 1422 (2d Cir. 1995). Since the UVTA and New York law no longer include this inquiry into the transferee's good faith, case law on "bad faith" has also diminished.

[105]See *In re TOUSA, Inc.*, 680 F.3d 1298, 133, 56 Bankr. Ct. Dec. (CRR) 135, 67 Collier Bankr. Cas. 2d (MB) 1035, Bankr. L. Rep. (CCH) P 82276 (11th Cir. 2012) (citing *In re Rodriguez*, 895 F.2d 725, 727, 22 Collier Bankr. Cas. 2d (MB) 633, Bankr. L. Rep. (CCH) P 73282 (11th Cir. 1990)).

[106]See *In re Northern Merchandise, Inc.*, 371 F.3d 1056, 1059, 43 Bankr. Ct. Dec. (CRR) 49, Bankr. L. Rep. (CCH) P 80112 (9th Cir. 2004) ("[T]he primary focus of Section 548 is on the net effect of the transaction on the debtor's estate and the funds available to the unsecured creditors.") (citation omitted); but see *In re Financial Federated Title & Trust, Inc.*, 309 F.3d

focus on the debtor's estate which makes up the funds available to unsecured creditors.[107] If courts are to apply this wider focus to uptier exchanges, it may come at the expense of the more tailored "dollar-for-dollar" approach for evaluating the value of antecedent debt.

Ultimately, lenders left out of an uptier exchange may have an uphill battle under present case law to the extent they pursue fraudulent transfer claims.[108] Bankruptcy and fraudulent transfer case law has not previously focused on the market valuations of debt exchanges and the attendant effects of such transactions on the debtor's estate. Still, with the rise of lender-on-lender violence, courts may have no choice but to address this issue soon.

1325, 1332, 40 Bankr. Ct. Dec. (CRR) 99, Bankr. L. Rep. (CCH) P 78735 (11th Cir. 2002) ("We conclude that a determination of whether value was given under Section 548 should focus on the value of the goods and services provided rather than on the impact that the goods and services had on the bankrupt enterprise.").

[107] *In re Jeffrey Bigelow Design Group, Inc.*, 956 F.2d 479, 484, 26 Collier Bankr. Cas. 2d (MB) 967, Bankr. L. Rep. (CCH) P 74478, 22 Fed. R. Serv. 3d 371 (4th Cir. 1992).

[108] While outside of the scope of this article, non-participating lenders have had success challenging uptier transactions on contractual or other grounds. See, e.g., Judge Finds Trimark Minority Lenders Assert Viable Claims Against Uptier Lenders Under 'Sacred Rights' Provisions, Make 'Plausible Argument' Exchange Required Unanimous Consent; Tortious Interference Claims Against Sponsors Centerbridge and Blackstone Dismissed REORG (Aug. 16, 2021) https://app.reorg.com/v3#/items/intel/11614?item_id=151841; Jonathan Schwarzberg, Tensions Rise as Private Equity-Backed Companies Push Limits REUTERS (June 15, 2018) https://www.reuters.com/article/pe-lending/tensions-rise-as-private-equity-backed-companies-push-limits-idUSL1N1TH0PY (discussing the uptier exchange in NYDJ).