

**New York University  
Leonard N. Stern School of Business**

**Corporate Bankruptcy & Reorganization  
FINC-GB.3198.10**

**Professor Edward I. Altman  
Professor James Peck  
Fall 2015 (1<sup>st</sup> Half)  
Thurs 6:00-9:00 pm  
Location: KMC 4-120**

This is a unique course in business administration curricula and has evolved in an interesting way over the past 40 years that Professor Altman has taught it and over the more than 30 years that Judge Peck has been practicing and teaching. The original focus was on discussing and using corporate distress prediction models from an external fixed income security perspective. These statistical-multivariate models, utilizing financial statement and market valuation variables, have become standard analytical procedures in the financial world, especially as financial institutions prepared for **Basel II and III**. They are now complemented by a number of newer analytical approaches, including option pricing and artificial intelligence models.

While the financial distress prediction aspect is still an important part of the course, perhaps the more important perspective is now (1) the valuation and analysis of distressed firms and their outstanding securities, primarily bonds and bank loans and how the bankruptcy process in both the U.S. and abroad has evolved. Indeed, this course can now be followed by a companion course on “*Distressed Securities, FINC-GB.3176*” (taught as an additional course in Spring 2015) as well as a Case and Prospectus Analysis course on “*Case Studies in Bankruptcy & Reorganization, FINC-GB.3199,*” (taught in Fall and Spring, 2<sup>nd</sup> Half). Discussion and analysis of the high-yield, junk bond and sovereign debt markets complement the distressed securities materials. Reorganization in bankruptcy cases explore this unique period in a company’s “life.” As a complement to the investment aspects of the course, we also pursue the financial and operating restructuring of ailing firms and the bankruptcy court environment that these distressed firms operate in. All full-time students are given the opportunity to join the NY Chapter of the *Turnaround Management Association* at a highly discounted price. Membership is, of course, open to all students.

Judge Peck approaches the subject matter of the course from the perspective of a seasoned restructuring professional and a retired bankruptcy judge who presided over the Lehman Brothers Chapter 11 and SIPA cases. His unique experiences include serving as mediator in the American Airlines, Residential Capital and General Motors cases. His teaching draws on these experiences and stresses the issues and uncertainties that tend to dominate restructuring negotiations – the fight for control, strategic posturing and differing perceptions as to value.

The pedagogy of the course includes traditional lectures, case studies, a guest speaker on turnaround management and corporate restructuring and “vulture” investing and a term paper related to the theme of the course. The latter project is discussed early in the course but is not due until almost the full semester is over. Students have the opportunity to present the findings of their term projects in a special, extra session at the end of the term. Incidentally, Stern has

“hatched” at least five-dozen vulture investors and traders of distressed securities over the years and this course is oftentimes the “breeding ground” for these successful “birds.”

## Course Outline

### I. General Course Description & Objectives

An in-depth study of practical and theoretical financial aspects and implications of corporate bankruptcy, credit analysis, and leveraged and distressed restructurings. Among the topics discussed are the bankruptcy-reorganization process; techniques and procedures to value firms in distress and/or reorganization; global implications of credit risk, predicting impending problems of various types of companies including manufacturing firms, retailers and commercial banks; the effect of bankruptcy on total share valuation; investment strategies relevant to distressed companies’ securities; financial restructuring; high yield “junk” bonds; the emerging-market corporate debt market; and the implications of bankruptcy analysis to financial lending institutions and non-financial corporate management personnel. References will be made to recent corporate failures and cases as well as to empirical and theoretical scholarly and professional studies.

### II. Course Requirements & Instructions

The pedagogy of the course includes seminar-type discussion of issues and latest research in the field, analysis of case studies, guest speakers, and student presentations of their case-research reports. The **major written requirement** will be an in-depth report of a significant corporate bankruptcy or a paper related to the theme of the course. Students are required to work in small **groups of two to four members**. See partial list of bankrupt firms and paper themes attached. Participants of the course are responsible for the required readings of each session’s discussion.

### III. Additional Practitioner Presentations

There will be one or two practitioner presentations on class-related subjects. These presentations will be held during the semester in our section and also in Professor Altman’s morning section on Tuesday or Thursday, 10:30-11:50am in KMC 2-80. You are invited to attend or can view these sessions on the class streaming videos (schedule will be distributed in class).

## Required Materials:

- A. Edward I. Altman and Edith Hotchkiss, **Corporate Financial Distress & Bankruptcy**, 3<sup>rd</sup> ed., John Wiley & Sons, 2006.
- B. Packet of Powerpoint Handouts and Exhibits (download from Blackboard)
- C. **Suggested books** - If “Investing in Distressed Securities” and/or “Managing Credit Risk” is very important to you, the following books are recommended:
  - a. J. Caouette, E. Altman, P. Narayanan & R. Nimmo, **Managing Credit Risk: The Great Challenge For Global Financial Markets**, 2<sup>nd</sup> edition, John Wiley & Sons, 2008
  - b. E. Altman, **Distressed Securities: Analyzing & Evaluating Market Potential & Investment Risk**, Probus, 1991, reprinted by Beard Books, 1999
  - c. S. Moyer, **Distressed Debt Analysis**, J. Ross, 2005
  - d. H. Rosenberg, **The Vulture Investors**, 1<sup>st</sup> or 2<sup>nd</sup> edition, John Wiley & Sons.

## IV. Detailed Course Outline

### Session

### Dates Subject and Readings

#### 9/17 **The Corporate Bankruptcy Phenomenon (EA)**

- Introduction to Corporate Financial Distress
  - Factors that cause firms to enter distress
- Business failures and Bankruptcies – Chapter 1
- Defaults and bankruptcies in 2000-2015
- Credit crisis of 2007-2009 (Global), 2009-2015 (Euro-Sovereign)
- Valuation theory in a distressed reorganization – review basic concepts
- Investing in Distressed Securities and High-Yield Debt: A Primer

#### **Overview of the Bankruptcy “Industry”**

- Major Players in the reorganization process
- The Chapter 11 process – Chapters 2, 4
- **Guest Speaker – Allen Kadish, President, NY Chapter of the Turnaround Management Association**

#### **Discussion of Team Projects**

#### 9/24 **The High-Yield Bond, Sovereign Debt and Distressed Debt Markets – Chapters 8, 9 and NYU Salomon Center Reports (EA)**

- Evolution and current status of the markets

- Risk and return analysis
- High-yield bonds and leveraged loans: the raw material for the distressed debt market
- Traditional default and mortality rate methods for estimating probability of default
- Recovery rate analysis
- Comparing 2007 with 2015 – credit markets: Is it a Bubble?
- Collateralized debt obligations
- Size, scope, players and evolution of the distressed debt market

10/1 **Credit Scoring Models: Predicting Financial Distress (EA)**

- Z-Score, Z''-Score and Z-Metrics analysis – Chapters 11 & 12 in text
- KMV, Neural Networks, etc.
- Enron/WorldCom and GM/Ford discussion
- For emerging markets-expanded version of Z''-Score – Chapter 12
- The rating agency industry – changes after the crisis?

10/1 **Implications & Applications of Financial Distress Prediction Models**

- For investors – Chapter 13
- For bankers – Chapter 13
- For managers – the corporate renewal process – Chapter 14
- The GTI Corporate Turnaround – Chapter 14
- How to avoid Chapter 22

10/1 **Sovereign Risk Analytics – Predicting Sovereign Default**

- Bottom-up approach
- Is the Euro crisis over?
- Next trouble spot?

10/8 **Transactional Risks Financing, Sale and Use of Property (JP)**

- Automatic stay
- Ipso facto clauses
- Avoidance powers
- Executory contracts
- Equitable subordination and claim priority
- Debtor in possession financing
- Sale of operating business without a reorganization plan
- Lehman and Chrysler

10/15 **Guest Speaker on Corporate Debt Restructurings from an IB Firm Perspective: Tim Coleman, Head of Corporate Restructuring, the Blackstone Group (EA & JP)**

- Investment bankers and turnaround management
- Valuation in bankruptcy
- Current issues, hot-areas and career opportunities

10/15 **Current Issues and Proposals on Revising fhs Bankruptcy Code (JP)**

**Avoiding Chapter 22 – is it Desirable? (EA)**

10/22 **Chapter 11 Plan of Reorganization (JP)**

- Plan support agreements and fear of free fall bankruptcies
- Prenegotiated or prepackaged plans
- Plan mediation to overcome negotiating blockage
- The rise and role of the “ad hoc” committee – EFH as example
- Material non-public information – ResCap as example
- Confirmation, capital structure and feasibility

10/22 **Cross Border Issues**

- Nortel joint trial and conundrum of judicial consistency
- Lehman protocol

12/17 **Student presentations on December 17 of term reports: all reports due December 17 (Incompletes are possible).**

- Attendance mandatory for all students, unless conflicting with other courses.

**Grading:** Will be based primarily on the term project with smaller weights for in-class contribution. Term project discussed in class (see sample of possible topics listed below).

**Office Hours/Location:** Professor Altman  
Thursday: 2:00 – 4:00 p.m.  
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## POSSIBLE BANKRUPTCY PAPER TOPICS

### Sample Themes

Abuses of the Bankruptcy Code  
Accountants' roles in bankruptcies  
Airline deregulation & bankruptcies  
Airline industry prediction model  
Argentina bank crisis  
Asset management companies (AMCs)  
Auto Supply & Automotive Industry  
Banking industry model  
Bankruptcy in the telecommunication industry  
Bankruptcy as a business strategy  
Bankruptcy and pension plans (PBGC)  
Bankruptcy expert systems  
Bankruptcy in Central and Eastern Europe  
Busted convertibles  
Chapter 22s, 33s, 44s  
China's bankruptcy Laws & NPLs  
Claims purchases as a takeover technique  
Climate change and the Insurance Industry  
Computer and Electronic Industry  
Corporate abuses and bankruptcy  
Crisis in Japanese banking  
Critical events analysis and bond price reaction  
Debtor-in-possession (DIP) financing  
Distressed Firm Control Strategy  
Distressed Ratio  
Emerging market corporate debt models  
Emerging Equity Investing  
Equity Performance in Reorganization  
Equity performance after bankruptcy emergence  
European Distressed Debt Market  
Fallen angels (e.g., GM & Ford)  
Financial reporting consolidation (captives) & Z-Scores  
Fraudulent conveyance  
Government Intervention & Creditor Rights  
Greece and the Euro-Peripherals  
Hedge Funds as Corporate Lenders  
Highly leverage transactions (HLT)  
Indirect and Direct Bankruptcy Costs  
Investing in bankrupt equities  
Japanese Rating Agencies  
LBO Bankruptcies  
Macro-default models  
Macro-influences on defaults  
Municipal defaults  
New Bankruptcy Act of 2005  
Option pricing default models  
Power companies and public utilities  
Pre-packaged bankruptcies  
Rating Agencies  
Rating downgrade triggers  
Roll-Up Strategy from Bankruptcies  
Sovereign Risk Models  
Subprime Mortgage Crises  
Systemic Risk Analysis  
Telecommunications industry prediction model  
The Corporate Bankruptcy restructuring industry  
The new BIS regulation on credit assets (Basel 11)  
Z-Scores and investing

### Sample Companies

Adelphia  
American Airlines (AMR)  
Bethlehem Steel/International Steel Group  
Borders  
Braniff International (Chapter 33)  
Caesar's Entertainment  
Charter Communications (Chapter 22)  
Chrysler  
CIT Financial  
Collins & Aikman  
Continental Airlines (Chapter 22)  
Dana Corporation  
Delphi Corporation  
Delta Airlines/Northwest  
Dow Corning  
Dynergy Corp.  
Eagle Picher Industries  
Eastman Kodak  
Energy Future Holdings  
Enron Corporation  
Euro Tunnel (1 and 2)  
Exide Corp.  
Federated Dept. Stores  
General Growth Properties  
General Motors/Ford  
Global Crossing  
Globalstar  
Grand Union (Chapter 33)  
Great A&P Tea Company  
Greyhound  
Hawker Beechcraft  
Hostess (Chapter 22)  
ICO Global Communications  
Kmart/Sears  
Lear Corp.  
Lehman Brothers  
LTV (Chapters 11 and 22)  
Lyndell Chemical  
MIF Global  
MGM Holdings  
Mirant Energy  
Montgomery Ward  
Nortel Networks  
Parmalat  
Patriot Coal  
Polaroid/Eastman Kodak  
Quebecor World  
R. H. Macy & Company  
Radio Shack  
Residential Capital  
Smurfit-Stone Container  
Swissair  
Tower Automotive  
Tribune Co.  
Trump Hotels & Casinos (Chapter 44!)  
United Airlines/Continental  
US Airways (Chapter 33?)  
Visetron  
Walter Energy  
Winn-Dixie Stores  
WorldCom