Distressed Governance Tracker

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Proper Governance = Deal Certainty + Max Value

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In re: CII Parent, Inc., Case No. 22-11345 (LSS) (Bankr. D. Del. April 12, 2023) (Silverstein, C.J.)

In This Article

RULING

Prior to commencement of a chapter 11 case, a secured lender exercised irrevocable proxies provided under its prepetition credit agreement with respect to certain operating companies (the "Opcos"), pursuant to which the secured creditor (i) amended the corporate governance documents and (ii) removed/replaced the managers and board. The debtor, the holding company of the Opcos, commenced the chapter 11 case for the express purpose of challenging the proxies, alleging that the proxies were improper and, if proper, were improperly exercised. In a fact specific ruling addressing the language of the applicable documents and a stipulated record, Judge Silverstein rejected the debtor's challenge and validated the secured lender's rights and the prepetition exercise of the proxy rights.

RESTRUCTURING LESSON

Well drafted and properly exercised proxy pledges will provide certainty to the bargained-for debtor/secured creditor relationship. The decision in CII Parent provides valuable guidance to debtors regarding strategic decisions to consider while in default, including, without limitation, the importance and integrity of forbearance agreements, negotiating leverage and timing, amendments to credit agreements and corporate organizational documents, and the benefit of a preemptive chapter 11 proceeding.

ANALYSIS

In the context of a motion to enforce the automatic stay, the debtor sought a declaration from the Bankruptcy Court that the secured creditor had not properly exercised proxy rights that were pledged at the time of execution of the prepetition credit agreement and exercised 6 days before the

ANALYSIS *Cont.*

commencement of the chapter 11 case. The Debtor argued that the secured creditor's refusal unwind the proxy exercise represented a violation of the automatic stay. Rather than pursue a summary proceeding under section 225 of the DGCL, the parties elected to proceed in Bankruptcy Court on a stipulated factual record.

While acknowledging that Delaware state courts narrowly construe the concept of irrevocable proxies, the Court reviewed the "documents as a whole" (the proxy, credit agreement, collateral agreement, and guarantee) and concluded that (i) the secured creditor was properly appointed as the debtor's proxy, (ii) an event of default existed (and was stipulated) at the time of exercise, (iii) the proxy was properly exercised and noticed by the secured creditor, and (iv) the 3-year statutory proxy duration was validly extended by agreement of the parties until the debt was paid in full. Judge Silverstein concluded that this "conclusion is consistent with the entire thrust of this commercial transaction, which is that the Collateral, including the Pledged Equity, secures Debtor's repayment obligations." Id at 21.