

Turnaround quarterback

Understanding the role lawyers play in a turnaround situation

INTERVIEWED BY ADAM BURROUGHS

A lawyer is an integral part of a turnaround team, uncovering legal issues in a way that allows the financial and business advisers to find the best path to turn the company around.

“It’s not the lawyer who is responsible for finding a turnaround solution, but rather he or she serves as a translator between the financial and business professionals, and someone who can assemble and lead the team that ultimately puts together the turnaround strategy,” says Gary Philip Nelson, a shareholder at Sherrard, German & Kelly, P.C.

Smart Business spoke with Nelson about company turnarounds, and what and who should be involved.

What are the first steps in a turnaround?

A key aspect of working with a troubled company is understanding what the lender is trying to accomplish and how it views the borrower; is it just an asset to be managed or is the loan part of an ongoing business relationship between the two?

A lawyer will consider relevant documents pertaining to loans and will do a lien search to see who, if anyone, has judgments or security interests in the debtor. Then the lawyer will assemble and analyze those loan documents, looking for leverage to negotiate more favorable results. A company that owes money and does not have much equity or personal resources will often take whatever it can get from a lender. A company with leverage can have a more even exchange because a vulnerable lender will recognize its vulnerability and try to contain its exposure by giving something up to fix the problem.

With the nature of the relationship understood, a lawyer can help the company find the right set of professionals to identify the problems and lead the turnaround.



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When is bankruptcy a more viable option?

Because the cost of Chapter 11 is now very high, the tendency is to attempt a non-bankruptcy court solution through a forbearance agreement, a state court receivership, or other non-bankruptcy solutions that are now more popular because they might be faster and less expensive. These alternatives give companies more control than going through court where creditors have a say or can band together in a lawsuit. They also allow banks and management to focus on the core problem and have a fighting chance to solve it.

A Chapter 11 proceeding can come into play, however, if the company gets into a situation in which it would be profitable if it were not buried in litigation or facing a large volume of personal injury or product liability lawsuits. Going into bankruptcy in these instances could result in the creation of personal injury settlement trusts for the benefit of tort victims, which offer protection to the post-bankruptcy company from mass tort plaintiffs.

What are the unique skills lawyers bring to turnaround situations?

When there are competing liens against a company’s assets, the lawyer can weigh in on who has the first priority so that everyone involved can focus the turnaround discussions on the right parties. If there are

liens that exceed the value of the collateral, the company may need bankruptcy to wipe them out because whoever holds them won’t voluntarily give up a lien position, even if there is no value.

Generally, officers and directors owe fiduciary duties to a narrow range of stakeholders. But, in certain jurisdictions, when a company is insolvent, the stakeholder group might expand to include creditors and employees, and result in an expansion of the fiduciary duties of managers and directors to include more constituents. Knowing this, and depending on who is the engaging client, experienced insolvency counsel can help managers or directors take appropriate actions to make a workout successful.

One of the more intricate areas in which a lawyer can help is with employment relationships, such as understanding the company’s responsibilities in collective bargaining agreements, whether it can lay off workers without notice, and what sorts of severance arrangements exist under current employment contracts.

A lawyer equipped with the necessary skills in this field can quarterback a turnaround situation, recruiting the help of service professionals and assigning them tasks while advising a company on whether an out-of-court or in-court solution is the best path. They are a vital part of the process. ●

WHEN YOUR COMPANY IS FACING A FINANCIAL ISSUE, KNOWING THE RIGHT PLAYS TO RUN IS CRITICAL.



At Sherrard, German & Kelly, P.C., the approach to the practice of law is simple and direct: We provide responsive, high-quality and cost-effective legal services to help our clients deal with financial issues in a way that allows management to take the right steps toward successful results.



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