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Bankruptcy filings dip

Premium content from Philadelphia Business Journal - by Jeff Blumenthal, Staff Writer
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Local Chapter 11 business bankruptcy filings fell close to pre-recession numbers in the first quarter after spiking dramatically between late 2008 through the middle of last year.

But a second wave of filings could come if interest rates rise without being accompanied by significant economic improvement, analysts and bankruptcy lawyers say.

Business Chapter 11 filings in New Jersey and the Eastern District of Pennsylvania have been relatively steady despite the economic downturn because most major companies choose to file in Wilmington or New York. The recession-related increase in filings in 2009 and 2010 in the 3rd Circuit, which includes eastern Pennsylvania, New Jersey and Delaware, came largely from Wilmington, where many companies from around the country incorporate to take advantage of the business-friendly court structure.

The number of Chapter 11 business filings in the 3rd Circuit combined were only 114 in second-quarter 2008. But after [Lehman Brothers](#) went under in September that year, followed by the stock market collapse, filings skyrocketed to 408 in the third quarter, 626 in the fourth quarter and 621 in first-quarter 2009. They remained elevated for the remainder of 2009 and the early portion of 2010 before dropping significantly to just 213 in first-quarter 2011.

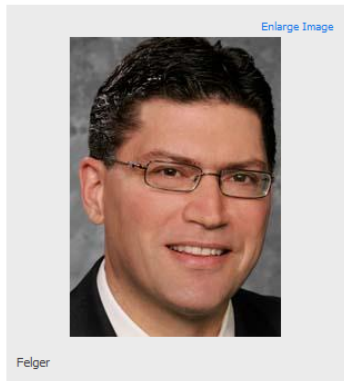
Cozen O'Connor bankruptcy department co-chair [Mark Felger](#), who also serves as the firm's Wilmington office managing partner, said there was a time in the first quarter of 2009 when his group was dealing with a filing every day in Delaware. But as the economy has improved slightly, he thinks businesses have become more optimistic about their standing.

"Lenders are more willing to lend, there are more opportunities for distressed companies to find liquidity sources and remain viable and existing lenders are more receptive to restructuring," Felger said.

[Stevens & Lee](#) bankruptcy department co-chairman [Robert Lapowsky](#) said in addition to businesses having more access to capital, some people in the industry theorize that borrowers were aided by loan agreements with few financial covenants, particularly commercial real estate loans. That means that borrowers can struggle but without defaulting.

But many filings that occurred in the most recent wave were pre-packaged arrangements with lenders that allow borrowers to reorganize. [Buchanan Ingersoll & Rooney](#) bankruptcy group chairman [William Schorling](#) said fewer midsize and small companies are using bankruptcy protection, choosing instead to either restructure their debt or sell the company. The reason for that is the fixed costs associated with bankruptcy that smaller companies cannot afford but larger ones can.

"It is costly, so smaller companies are selling assets or looking for a buyer," said [David Ferrara](#), a visiting instructor at [Villanova University's](#) School of Business. "The process of



Felger

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...FELGER, a visiting instructor at [Vanderbilt University's](#) School of Business. "The process of bankruptcy could take longer than they would prefer so they just sell for 30 cents or 40 cents on the dollar and then it becomes someone else's problem."

While the decline in business filings is viewed as a good sign for the economy, many pundits are predicting there will be another spike in filings when and if interest rates rise.

Schorling said many struggling businesses have been saved by "unrealistically low" interest rates that allow them to maintain reasonable levels of cash flow despite the prolonged economic slump.

Felger said he will enjoy the downtime for the next quarter or two because most pundits expect another spike.

"Interest rates could affect the liquidity of many companies that could go off the cliff unless they find favor with their lenders," Felger said. "[The Federal Reserve] is trying desperately to keep interest rates low but many question for how long."

Lapowsky said if interest rates rise as the economy improves, "that could make up for the additional borrowing expense. But if rates go up and the economy doesn't, there could be a problem."

The number of Chapter 11 business filings in Wilmington rose from just 45 in second-quarter 2008 to 306 in the third quarter, 531 in the fourth quarter, 449 in first-quarter 2009 and remained over 300 filings a quarter through first-quarter 2010. Since that period, filings have declined to just 93 in the first quarter of this year, the lowest number since second-quarter 2008.

Conversely, the number of Chapter 11 business filings in Pennsylvania's eastern district, which is based in Philadelphia, have not fluctuated much since the beginning of 2008 — from a low of 19 in second-quarter 2008 to a high of 45 in first-quarter 2009 to 28 in first-quarter 2011. Quarterly filings in New Jersey have ranged from 50 to 127, with 92 in the first three months of 2011.

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