Bankruptcy Court Can Be Tough Venue for Hostile Takeovers

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US Airways Chief Executive Doug Parker faces a major handicap in his $8 billion bid to acquire unreceptive Delta Air Lines Inc.: Bankruptcy courts tend to be poor staging grounds for hostile takeovers.

Unless Delta's management can be persuaded to go along with the deal or its creditors stage a revolt in the bankruptcy court, US Airway's bid is a longshot, bankruptcy experts said Wednesday. Delta has exclusive control over its Chapter 11 case through at least early February, and bankruptcy courts seldom overrule management when things are going smoothly.

Mr. Parker "basically lobbed this Hail Mary pass up in the air to see who's going to catch it," said Fulbright & Jaworski partner William Rochelle. "To be able to have a prayer for success, he's got to be able to generate interest from creditors."

Mr. Rochelle, who represents secured creditors in airline bankruptcy cases, said Parker chose the "least offensive method" to persuade Delta to accept its proposal. Rebuffed by Delta's management, he decided to publicly court the carrier's unsecured creditors, who stand to gain a 45% stake in what would be one of the world's largest airlines.

But Mr. Parker, the America West chief who took the helm of US Airways when it merged with the Arizona-based carrier last fall, could be in for a bumpy ride as he attempts to take over a company protected by the bankruptcy court.

"If management is hostile to the US Airways proposal, US Airways may find it difficult to force its way into the room," said Reed Smith bankruptcy partner Eric Schaffer, who worked on US Airways' first Chapter 11 case. US Airways emerged from its second bankruptcy reorganization in 2005.

Ray Neidl, an airline analyst with Calyon Securities Inc., said convincing Delta's major creditors will be crucial if US Airways wants this deal to work.

"If the creditors see a better proposal, then the management would probably have to listen to them," he said.

Resisting Us Airways' Advances
For now, Delta is still resisting US Airways' advances. Chief Executive Gerald Grinstein responded Wednesday with a terse statement, making it clear that the company still plans to move forward with a stand-alone reorganization and that it intends to invoke its control over its Chapter 11 case to do so.

"The bankruptcy court has granted Delta the exclusive right to create a plan of reorganization until Feb. 15, 2007," he said. "We will continue to move aggressively toward that goal."

Delta, the nation's fourth largest airline, sought Chapter 11 protection on Sept. 14, 2005, about a month before changes to the Bankruptcy Code that sharply curbed debtor control in Chapter 11 cases took effect. Accordingly, the airline can expect to continue to drive its own reorganization process even beyond the current Feb. 15 plan filing deadline.

Companies in Chapter 11 protection are given an exclusive period of time to file a Chapter 11 reorganization plan, but can seek extensions if negotiations with creditors are moving forward. Although last year's bankruptcy law changes limit those to a maximum of 18 months, Delta could potentially enjoy unlimited extensions -- as did UAL Corp., the parent of United Airlines, which spent more than three years in bankruptcy.

Creditors can seek to end a company's exclusive control over its Chapter 11 case so they can file their own reorganization proposals. But bankruptcy experts say Delta's creditors would face an uphill battle wresting control from a team of competent executives managing a viable company.

Over the last year or so, Delta has negotiated deals to terminate its pilots' pension plan, obtained $280 million in annual wage-and-benefit concessions from its pilots, and said it's "on track" to exit Chapter 11 proceedings by the middle of 2007. The airline has also recalled 1,000 flight attendants in preparation for a major expansion of its international routes.

"Bankruptcy courts don't terminate exclusivity easily or quickly," Mr. Rochelle said. "It takes a lot of banging on the door before things happen."

In the absence of a deal with management, convincing a pivotal group of unsecured creditors -- the official committee that represents them in the airline's Chapter 11 case -- will be key.

The panel, formed early in every Chapter 11 case and usually made up of the largest unsecured creditors, has significant influence in a bankruptcy case and can be instrumental in swaying the court to second-guess a debtor company's business judgment.

The Delta committee, which includes aircraft financier Boeing Capital Corp., the federal Pension Benefit Guaranty Corp., Bank of New York Co. and the Air Line Pilots Association, hasn't yet shown its hand. Calls to committee members and the attorney who represents them weren't returned Wednesday.

US Airways could choose to buy Delta's unsecured claims in order to gain a foothold in the case and command the committee's attention, a move potential buyers often employ in smaller Chapter 11 cases.

For example, the hedge fund Harbinger Capital Partners forced an exclusivity battle in the bankruptcy of West Coast jewelry chain Crescent Jewelers and ultimately won control of the company post-bankruptcy. Harbinger later merged the company with another company it bought out of Chapter 11 -- East Coast chain Friedman's Inc.

Financier Ron Burkle's Yucaipa Cos. has bought up unsecured debt of rival auto-hauling companies Allied Holdings Inc. and Performance Transportation Services Inc., which are both operating under Chapter 11 protection, and is expected to attempt to merge them post-bankruptcy.

US Airways, whose smooth merger last fall with America West had management backing, has the experience of two past Chapter 11 cases as it moves forward with its proposal.

The airline could ally itself with other major creditors to force Delta -- or the Manhattan bankruptcy court -- to move toward a merger.

"Management will have to consider what the creditors want," Mr. Neidl said. "It's the most important element of the company now, and they'll at least have to listen to their opinion."

But Mr. Rochelle of Fulbright & Jaworski said he'd be surprised if Delta and its major creditors "ran off in different directions."

He also questioned whether US Airways' Mr. Parker, widely regarded as a savvy executive who saved his airline from extinction, would want to be the architect of a deal built on a bitter battle between Delta and its creditors.

"I don't know whether Doug Parker would want to do it on a highly adversarial basis," Mr. Rochelle said. "That would really not create the kind of an effective working environment you need to integrate three airlines."