



Bankruptcy is Not the Only Way: Alternative Insolvency Techniques in Delaware

With many entities choosing to incorporate in Delaware, the state has become a center of cross-border insolvency disputes. Many parties (especially those outside the U.S.) assume a Chapter 11 bankruptcy is the best way to achieve their goals, but as our Insolvency and Delaware teams explain, there are alternatives that could be quicker and cheaper.

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Delaware's role as a favored U.S. state for the incorporation of entities has also made it a center of high-stakes, cross-border insolvencies. Parties (especially those from outside the U.S.) tend to assume that a Chapter 11 bankruptcy is the quickest way to achieve their end goals – however, corporate bankruptcies may be long, drawn-out, unpredictable and costly.

Below is a short list of alternative insolvency techniques in Delaware that are potentially quicker and cheaper than bankruptcy.

Delaware State Court Receivership

What is it? When the debtor has engaged in fraud, this approach generally involves a third party being appointed by a court as a fiduciary to take control over a business or asset for a particular reason, such as operating or liquidating the business for the benefit of creditors (to name one example).

Pros:

The Delaware insolvency receivership statute for corporations is well detailed, and the Delaware Court of Chancery is familiar with the procedures.

Any creditor or shareholder may request the appointment of a receiver of an insolvent corporation and the powers of a Delaware insolvency receiver are broad.

Because a Delaware receivership is flexible and the Chancery Court rules are subject to relief, it may be a much faster and cheaper alternative to a formal bankruptcy.

Cons:

The grounds for appointment of a receiver vary, and the appointment of a receiver is generally only granted where it serves some beneficial purpose not achieved by ordinary debt collection procedures.

Voluntary Dissolution & Winding Up

What is it? The process of closing down an entity and winding up its business affairs. This process typically involves (i) obtaining approval of the entity's board or shareholders and (ii) filing the requisite papers with the Secretary of State.

Pros:

A dissolution is quicker and more cost effective than other options.

The process is less formal than a Chapter 11 bankruptcy proceeding, with no formal meeting of creditors required.

The entity may continue to exist for limited purposes such as prosecuting or defending lawsuits and disposing of property.

Cons:

A dissolution can vary in complexity based on the nature and amount of distributable assets.

A dissolution is still vulnerable to legal challenges by objecting creditors and judicial intervention is possible.

Delaware's approach can either be overseen by a court or done voluntarily and without oversight, which differs from a winding up in English jurisdictions, which are overseen by a court.

Assignment for the Benefit of Creditors ("ABC")

What is it? A state law insolvency proceeding that assigns the debtor's assets to an assignee (like a trustee or insolvency administrator in other jurisdictions). The assignee then liquidates the assets for the benefit of the creditors (in order of priority).

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Pros:

ABCs are typically much faster than a bankruptcy proceeding and less expensive because it is a streamlined procedure with a limited purpose (to liquidate assets).

Cons:

Shareholder consent is often required, which may be difficult to obtain – a board vote alone cannot approve the filing of an ABC.

It does not discharge the debtor's obligations, and it is typically considered an event of default under other contracts.

In summary, there is no "one size fits all" insolvency technique in Delaware, and parties should choose the approach that fits their unique circumstances.

About Kobre & Kim

Kobre & Kim is a conflict-free Am Law 200 law firm focused on disputes and investigations, often involving fraud and misconduct.

Often working closely with lawyers in key non-U.S. markets around the world, our Delaware team:

Consists of experienced trial litigators in the Delaware Court of Chancery and U.S. Bankruptcy Court for the District of Delaware who focus on complex commercial disputes; Offers aggressive, creative and independent advocacy even in cases involving numerous, overlapping institutional stakeholders' interests because our firm avoids ongoing client relationships with common industry participants; Has significant experience in corporate governance matters, having led and defended initiatives on special investigative committees and steering committees of equity holders, served statutory notices and pursued emergency actions related to asset-freeze applications, applied for involuntary receiverships and liquidations, and pursued other special strategies to place our clients in a position of strength.