

Professional Profile.....

Renewal

Huron's Lukenda Helps Build a Practice by Saving Companies

by Dave Buzzell

Huron Consulting Group is one of the biggest names in the consulting business, but it wasn't always that way. In 2002, Huron was just one of the Great Lakes. As the story goes, the agreement that provided the start up funding for Huron was consummated in a restaurant on Huron Street in Chicago. Shortly after that, Huron was launched by 25 former Arthur Andersen partners. One of those was Jim Lukenda, who has been a mainstay of Huron's development as a turnaround and restructuring firm.



Jim Lukenda
Huron Consulting Group

Lukenda has been engaged in bankruptcy and restructuring consulting since the late 1980s, and since 2002 with Huron, as a New York-based managing director. "I was part of the original group that started Huron," Lukenda explains. "I left my office on March 10, 2002 as a partner in my old firm and returned on Monday morning, March 13, as a Huron managing director. The start-up of Huron was a very exciting time. My colleagues and I were engaged in a thrilling endeavor, starting a new venture from almost nothing."

Broad Expertise

Over time, Lukenda has worked with companies in a broad range of industries and represented just about every constituency – from boards of directors to management, equity investors, and creditors' committees. His specialty is turnarounds and reorganizations, but he has also been

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Innovative Solutions.....

Solyndra Salvaged

Investors Preserve Potential Tax Benefits of Company's Failure

by Randall Reese

Solyndra's fall from clean technology royalty to extremely expensive failure was quick and painful. Fremont, California-based Solyndra launched in 2005 with plans to manufacture solar photovoltaic power systems designed for large commercial and industrial rooftops. Over the next six years, the company would raise over \$1 billion in venture capital financing, receive the later-controversial \$535 million loan guarantee from the U.S. Department of Energy, and generate over \$250 million in sales.



Debra Grassgreen
Pachulski Stang Ziehl & Jones

However, by early 2011, Solyndra's situation was becoming dire. During calendar year 2010, the company generated a net loss of \$329 million on only \$142 million in sales. Moreover, oversupply of solar panels was driving down prices worldwide while governmental subsidies and incentives for the purchase of solar energy were ending, hurting demand for Solyndra's products.

On August 31, 2011, Solyndra suspended operations and terminated most of its workforce. Shortly thereafter, two Solyndra legal entities – parent holding company 360 Degree Solar Holdings, Inc. and wholly-owned operating subsidiary Solyndra LLC¹ – filed for Chapter 11 protection in Delaware in order to commence an orderly liquidation. During the cases, Solyndra failed to find a buyer for its assets on a turnkey basis, and financial advisor Imperial Capital estimated that there would be less than \$120 million generated by the liquidation of assets for

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involved in a good bit of forensic investigation work as well.

Lukenda was recently involved in winding down a marketer of over-the-counter health products. When one of the company's products was linked to a serious medical condition, he was brought in as CRO to obtain funding from the company's insurers for a plan of reorganization to complete a settlement negotiated with the plaintiff's counsel.

Lukenda was pleased with the outcome, noting that the creditors received 95 cents on the dollar on their claims. In the resulting reorganized company, Lukenda served as president while attempting to license some of the debtor's old trade names.

As an advisor to Northwest Airlines in its bankruptcy, Lukenda and his team collaborated with management on reporting and compliance matters. "Working with a top-notch management and legal team on a successful case is one of the reasons this work is so appealing," he said.

Northwest emerged from Chapter 11 a strong competitor and merged soon thereafter with Delta Airlines. More recently, Huron represented the Great Atlantic and Pacific Tea Company (A&P). Lukenda's role in that engagement was to develop a liquidation analysis in support of the "best interests of creditors" test required to confirm a plan of reorganization. Given the slim margins that were available to A&P and its creditors, Lukenda's analysis was a critical part of the A&P confirmation process.

His biggest case presently is WP Steel, also known as RG Steel. In this case, the Huron team is representing the official committee of unsecured creditors.

While his plate remains full, Lukenda has observed a change in the nature of his assignments. "There are fewer turnarounds occurring today in the restructuring environment. For those companies that end up in bankruptcy, such as RG Steel, there's not a lot of restructuring going on. In RG's case, basically, the company

was shut down and its assets sold for salvage value. Consequently, that leaves the parties in the case looking for sources of unrealized value. That, in turn, tends to lead to litigation – Chapter 5 causes of action, preference recoveries, fraudulent conveyance considerations. There's a great interest in turning over every rock and making sure potential litigation recovery is adequately addressed."

Lukenda's forensic skills were brought to bear in the demise of The 1031 Tax Group, which was taken into bankruptcy shortly after its offices were raided by the postal authorities. A tip had revealed that the principal had been misappropriating section 1031 tax exchange funds. Huron investigated the matter and marshaled the documents that were later turned over to the Chapter 11 trustee who pursued litigation against a number of banks and other parties that were complicit in the fraud.

to macroeconomic factors. "Oil and gas construction contractors went through a peak in 2007 and 2008. Then the economy fell off, leaving companies that were highly leveraged in difficult straits. My personal assessment is that while construction contractors can be 'cash cows', they don't lend themselves to good leveraged deals because of the large swings that occur in those markets."

The automotive sector also has lingering issues, says Lukenda, especially middle market OEM suppliers. He also anticipates a fallout from the ongoing dysfunction in the U.S. government, a subject that he recently wrote about in a white paper available on Huron's website. "There are numerous smaller private contractors in the government space, especially the defense industry, and the jury is out as to what's going to happen with the sequestration. The last time the Department of Defense

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Ebbs and Flows

Lukenda enjoys not only the changing nature of his engagements, but also the market ebbs and flows. "One of the things I have always found interesting in this line of work is its cyclical nature. Certain industries struggle, you spend some time with that industry, it stabilizes, and problems arise demanding attention with a new industry."

Lukenda points to the retail industry, which has gone through several cycles during his career. "My first time was in the early 1990s when many smaller retailers and catalog showrooms disappeared. In the last go-round, Wal-Mart put the stake in a lot of retailers. Right now, it is relatively quiet on the retail front, while there is a lot of work with companies in the energy sector."

According to Lukenda, oil and gas companies are very susceptible

had cutbacks, in the early 1990s, many government contractors went through restructuring. There was a real boom in defense-related M&A, with the stronger players picking up the weaker players."

On the Move

Lukenda began his career in public accounting in Washington, D.C. He transferred to New Jersey in 1985 as his wife, Maura, was completing graduate school with job prospects in New York City. A PhD in industrial psychology, she is the brains in the family, said Lukenda. They now reside in Montclair, New Jersey, with their two children, Maggie and James.

Lukenda enjoys the outdoors, and last September joined some high school classmates for a four day reunion hike in the Cascade Mountains of Washington state. "It was a great

experience to get out again and be with old friends," he said. "There are some opportunities to hike and camp in the Adirondacks and the Catskills here on the east coast, but nothing like the Cascades."

When not on the road, Lukenda commutes from Montclair to Huron's New York office. He is proud of the restructuring and turnaround operation Huron has built since its founding. "We have assembled a team of young, smart people with excellent skills, who are knowledgeable about business, restructuring, and the bankruptcy environment."

"One attribute that Huron brings to our clients is the experience of working on cases on behalf of different parties," said Lukenda. "It's the perspective of how the other side is thinking, which you may not find with a firm that is focused only on

debtor work or creditor work. Having that perspective is one of the things I find is critical to achieving consensus."

Building a Practice

Lukenda said that when Huron first started its restructuring practice it was like a three-legged stool with only two legs. Debtor and creditor advisory work alone left a missing balance to the practice. The one leg it was missing was the turnaround/crisis management aspect of the business, which it addressed when it acquired Glass & Associates in 2007. John DiDonato, who came over from Glass, runs Huron's restructuring practice today, taking over from Lukenda, who was the interim leader in 2006. He was happy to turn over the reins. "I didn't see it as one of my skill sets to be a long-term practice

leader. When John and the rest of Glass & Associates joined us, it was a very successful acquisition for our restructuring group."

Huron has had a series of successful acquisitions over the years, and the company has grown from 200 to more than 2,000 employees today. "I look back at the last ten years here at Huron and I am amazed at what we've been able to accomplish. As Huron overall has grown and become a force in healthcare, legal, and other areas, our restructuring practice has managed to maintain its position in some very difficult market cycles. While some of the excitement of those early start-up years has diminished, the ever-changing opportunities that present themselves and a great team of colleagues make it easy to get up each morning and head out to meet the next challenge." □

Solyndra...

distribution to Solyndra's creditors.² By comparison, Solyndra's secured and unsecured creditors were owed nearly \$800 million and as much as \$135 million, respectively.

Solyndra did have one other group of assets that could be of very significant value to a very limited group of parties, however. As a result of its history of losses, Holdings held net operating loss (NOL) carryforwards for U.S. federal income tax purposes. In court filings, Holdings estimated that those carryforwards would "total between \$875 million and \$975 million after emergence from bankruptcy."³ Based upon assumptions that a reorganized Holdings could generate sufficient income before expiration of those tax attributes against which they could be applied, Holdings further estimated that they could generate future tax savings of as much as \$341 million.

However, in order for those tax benefits to be realized in the future, certain criteria would have to be met. Most obviously, Holdings would have to be reorganized and continue to exist such that it could generate

future income against which the tax benefits could be offset. Certain sections of the Internal Revenue Code present additional hurdles. First, section 382 of the Internal Revenue Code severely limits the ability of a corporation to use its NOL carryforwards to offset future income if the corporation experiences a change in ownership.⁴ Second, section 269 of the Internal Revenue Code limits the use of NOL carryforwards in the event that an acquisition of control occurs.⁵ Therefore, the Internal Revenue Code essentially served to limit the use of Holdings' NOL carryforwards unless its existing equity holders were to retain substantially similar ownership stakes post-reorganization.

As laid out earlier, Solyndra's liabilities dramatically exceeded even the top end of its likely recovery range on the sales of its assets. The result was that secured creditors stood to receive only pennies on the dollar and unsecured creditors appeared to be left out in the cold. Because a class of creditors that receives nothing under a plan of reorganization is deemed to reject such plan, the "fair and equitable" standards of section 1129(b) of the Bankruptcy Code would apply and prohibit any

junior class of claims or interests from receiving or retaining any property of value. The estimated \$27 million of general unsecured claims against Holdings would therefore be expected to preclude the retention by Holdings' existing equity holders of their existing equity interests and, thereby, the realization of any value from Holdings' NOL carryforwards.

But that didn't happen. Instead, the companies' largest pre-petition equity holders, who were also lenders to the companies, agreed to fund a Chapter 11 plan process in exchange for a series of interrelated settlements that would allow them to retain their equity in Holdings and at least potentially preserve its valuable tax attributes.

"The development of the plan took place over several months and involved negotiations between the debtors, the creditors' committee, plan sponsors, landlords and the WARN claimants," according to Debra Grassgreen, a partner at Pachulski Stang Ziehl & Jones LLP, which represented Solyndra in the bankruptcy cases. She also noted that "the decision to have the holding company survive and retain its tax

attributes was not an isolated one – it was part of a global discussion.”

The plan of reorganization embodying the settlements, which funded at least a small recovery for general unsecured creditors, was overwhelmingly accepted by each class of creditors entitled to vote, except for two. The only voting creditor in the two rejecting classes was the U.S. Department of Energy. The most strenuous objections to the plan also came from governmental entities, with an objection of particular interest coming from the Internal Revenue Service.

The IRS argued in court filings that the plan of reorganization was unconfirmable because its principal purpose was tax avoidance through the preservation of Holdings’ NOL carryforwards. The agency’s objection made much of the fact that the plan would liquidate Solyndra LLC – which was the only entity with active business operations and employees immediately prior to the bankruptcy filing – and leave Holdings to emerge with neither employees nor active business operations. In addition, the IRS argued that one of the plan sponsors had recently valued its share of Holdings’ tax attributes at “17 times the amount of its \$4.5 million contribution to the Plan.”

In contrast, confirmation of the proposed plan was supported by the creditors’ committee, the debtors, and the plan sponsors. In responding to the objection of the IRS, each emphasized that the settlements that led to the consensual plan benefited creditors and provided general unsecured creditors with at least some recovery for their claims. While they acknowledged that preservation of tax attributes was a goal of the plan, they asserted that it was not inconsistent with section 1129(d) of the Bankruptcy Code because it was not “the principal purpose” of the plan.

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butes provided additional value to the plan sponsors which was helpful in encouraging them to support the plan as a whole,” said Grassgreen. The parties also noted that the plan was not creating new tax attributes, but merely preserving potential tax attributes that existed prior to the bankruptcy filing.

At the conclusion of the contested confirmation hearing held on October 22 of last year, Judge Mary Walrath rejected the IRS’s contention and confirmed the plan over its objection. In her oral ruling, she noted that the plan of reorganization dealt with many issues other than just the preservation of the tax attributes and that, for section 1129(d) to be violated, tax avoidance “has to be the primary, most important purpose of the plan.” Judge Walrath rejected the position that the plan sponsors’ knowledge of the tax attributes and desire to structure the plan so as to retain them meant that the plan’s primary purpose was tax avoidance. Finally, she highlighted that the plan did not “eliminate any rights the IRS may have to assert that the NOLs cannot be utilized under the Internal Revenue Code, at the time that the reorganized debtor seeks to use them” and stated that she viewed “the plan and the confirmation order as neither enhancing nor affecting any of the rights of any of the parties to the NOL.”

While Judge Walrath’s ruling was, in Grassgreen’s view, consistent with existing legal precedent, the court’s opinion “will be a helpful guide in other cases with similar facts.” In particular, the opinion affects the

restructuring of “early stage (start-up) companies and may impact whether a wind down or restructuring is accomplished in or out of court.”

“The case is a good reminder to practitioners that often there are non-tangible assets, such as tax attributes, that should be considered to determine whether additional value can be generated for creditors,” said Grassgreen. “It’s a reminder to think out of the box.” □

Notes

¹ For clarity, the term “Solyndra” will be used in this article to refer to the two companies collectively. The term “Holdings” will be used to refer to 360 Degree Solar Holdings, Inc. individually and the term “Solyndra LLC” will be used to refer to Solyndra LLC individually.

² Solyndra’s assets also included potential recoveries under an anti-trust complaint filed against three Chinese solar manufacturers which sought \$1.5 billion in damages for “illegal dumping of solar products and other anti-trust violations, anti-competitive practices, and tortious conduct.” That complaint was filed in the United States District Court for the Northern District of California on October 11, 2012.

³ Solyndra also claimed general business credits for research and development totaling approximately \$12 million. For simplicity, this article refers primarily to the net operating loss carryforwards.

⁴ For purposes of section 382, a change in ownership is generally deemed to have occurred if the percentage of stock of the corporation owned by one or more five-percent shareholders has increased by more than 50 percentage points over the lowest percentage of stock of the corporation owned by the shareholder at any time during the relevant testing period.

⁵ For purposes of section 269, an acquisition of control generally occurs if a person acquires ownership of stock representing at least 50 percent of either the total combined voting power or the total value of a corporation’s stock.

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