

SELECTED POST-BAPCPA KERP DECISIONS

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Dana I

Key Facts:

- Chapter 11 Debtors sought authorization to enter into employment compensation agreements with six key executives.
- The Debtors sought approval to pay base salary, annual incentive plan (“AIP”) bonuses and “target completion bonuses” to each of these six executives.
- Under the AIP, annual bonus was to be conditioned on the company’s short-term financial performance and the size of the award would depend on whether the company met certain performance goals. The “target completion bonus” involved both a fixed and variable component. The fixed component would be awarded without regard to performance and payable in cash on the effective date of a plan for reorganization so long as the executive was still employed by the company, while the variable part was to be based on “Total Enterprise Value of the Debtors” six months after the effective date.
- The Debtors also proposed to pay executives who were involuntarily terminated certain “payments in exchange for non-compete agreements.”

Holding:

- The Court denied the request for approval, in part, on the grounds that “[t]he Completion Bonus includes an amount payable to the Executives upon the Debtors’ emergence from chapter 11, regardless of the outcome of the cases.” Further, the Court stated that “[w]ithout tying this portion of the bonus to anything other than staying with the company until the Effective Date, the Court cannot categorize a bonus of this size and form as an incentive bonus.” The Court went on to provide, “[u]sing a familiar fowl analogy, this compensation scheme walks, talks, and is a retention bonus.”
- The Court also declined to approve the payments to executives upon involuntary termination, finding that it was essentially a severance payment and violated §503(c)(2).
- While disapproving the Debtors’ compensation proposal, the Court left open the possibility for a revised plan, stating “it may be possible to formulate a compensation package that passes muster under section the 363 business judgment rule or section 503(c) limitations,” and “incentivizing plans which may have *some* components that arguably have a retentive effect” do not necessarily violate section 503(c).

Dana II

Key Facts:

- Following the order denying the Debtors' first motion, the Debtors modified their compensation proposal and moved for reconsideration.
- In this second proposal, the Debtors modified the plan so as to require certain benchmarks for the executives to receive bonuses. In discussing the benchmark for the long term performance based incentive, the Court noted "the benchmarks for the LTIP are difficult targets to reach and are clearly not 'lay-ups.'"
- The revised proposal did not contain any guaranteed payments to the CEO or senior executives, other than base salary, simply for staying at the company through confirmation.

Holding:

- The Court approved the modified compensation plan, although it imposed a yearly ceiling on senior executives total compensation.
- In so holding, the Court stated, "[b]y presenting an executive compensation package that properly incentivizes the CEO and Senior Executives to produce and increase the value of the estate, the Debtors have established that section 503(c)(1) does not apply to the Executive Compensation Motion."

Nobex Corp.

Key Facts:

- The Debtor entered bankruptcy to sell assets under § 363. The Debtor moved to pay "sale-related incentive pay" to two senior managers.
- The "incentive pay" would only be paid if the gross sales price exceeded the stalking horse bid, and the amount of such pay would depend on the extent of which the gross price exceeded the stalking horse.

Holding:

- The Debtor's motion was granted.
- The "sale-related incentive pay" was not proposed to induce the managers to stay with the company; but rather, to incentivize them to "maximize the value of the Debtors' assets." As such, the "sale-related incentive pay" was not prohibited under section 503(c).

Global Home Products

Key Facts:

- The Debtors sought approval to implement a “performance and incentive based bonus plan” and a “incentive based sales bonus plan.” The plans required, at least in part, that certain goals be met, such as minimum EBITDAR.
- There was evidence presented that the plans were nearly identical to plans previously in existence at the Debtors in prior years.
- A labor union objected to the Debtor’s proposal. The creditors committee initially objected but subsequently withdrew its objection. The prepetition bank lender and the DIP lenders supported the plan.

Holding:

- The plans were approved.
- The Court focused on whether the plans were “pay to stay” plans or “pay for value” plans.
- The Court held “the Plans are primarily incentivizing and only coincidentally retentive because Debtors employed virtually identical plans prepetition when retention was not the motive.” Because the plans are primarily incentivizing, they are not subject to the restrictions set forth in §503(c).
- The Court found that the “[t]he Plans are clearly in ordinary course of the Debtors’ businesses,” noting that they are consistent with industry standards and with the Debtors’ own past practices.
- The Court analyzed the plans under a deferential “business judgment test” and approved them.
- The Court rejected the union’s argument that the bonus plans were inconsistent with the notion of “shared sacrifice,” finding that by motivating management and sales people to create additional value, all constituencies would benefit.

Calpine

- Key Facts:
- The Debtors sought approval of a compensation plan, entitled the Calpine Incentive Program (“CIP”), pursuant to section 363(b) and 503(c)(3).
- The CIP had four components -- (i) the emergence incentive plan; (ii) the management incentive plan; (iii) the supplemental bonus plan; and (iv) the discretionary bonus plan. The Debtors also wanted to assume the “CEO Agreement” and enter into a “CFO/CRO

Agreement”; both agreements included one-time signing bonuses and various performance and success fee bonuses.

Holding:

- The Debtors’ request was granted.
- The Court found that these were incentive plans which were designed to enhance the value of the estate. In so holding, the Court noted “[t]hey are not retention plans, although anyone can always make an argument that if people are made happier than they were before, then they would be excited to stay with the company, but that’s not the focus of these plans.”

Nellson Nutraceutical

Key Facts:

- Prior to filing bankruptcy, the Debtors had implemented a KERP for nine management employees.
- Almost immediately after the chapter 11 filing, the Debtors implemented two separate incentive plans for certain employees. The first was a management incentive plan (“MIP”), which replaced the KERP. The second was the ordinary course employee bonus compensation program (the “OCP”).
- The Debtors did not seek Court approval of the OCP before implementing it, but during a hearing on the MIP the Debtors told the Court that they would seek Court approval prior to making payments under the OCP, in the event the performance milestones described in the OCP were not met.
- As it turned out, because the Debtors did not achieve the milestones that would have triggered bonus payments under the OCP, the Debtors sought to modify the OCP to authorize paying bonuses to the employees covered under the plan, even where such bonuses would not have been due under the prior targets.
- The US Trustee opposed the modification motion.

Holding:

- The Court found that modification of the OCP was within the ordinary course of the Debtors’ business.
- The Court determined that the Debtors’ proposed modification of the OCP was in the ordinary course of the Debtors’ business. As a result, the Court held that §503(c)(3) does not apply because that section applies only to payments outside the ordinary course of business.

- Further, the Court found that that the bonus payments under the modified OCP were “not for the primary purpose of inducing the [] employees to remain with the Debtors’ business and, thus, they are not precluded or restricted by section 503(c)(1) of the Bankruptcy Code.” In addition, the Court noted that “[u]nder the facts of this case, although the modification of the 2006 bonus program has some retentive effect, it is for the primary purpose of motivating employees and, thus, the limitations of section 503(c)(1) are not applicable.”