

Bankruptcy of General Motors

Christopher Bosco and Catherine Plante

Abstract: The bankruptcy of General Motors was historical, not only because of the size but also because of the political nature of the process. The federal government was influential in the process which provided an outcome unique in the history of bankruptcy. This paper explores the implications of the General Motors bankruptcy on stakeholders especially those who unknowingly were exposed to risk. This paper puts into perspective how detrimental major bankruptcies can be, and it refutes the notion that only those who take a calculated financial risk are the only ones adversely affected by a bankruptcy.

Keywords: bailout, bankruptcy, General Motors, restructuring

1. Introduction

In 2008/2009, General Motors, one of the world's largest automakers, was on the verge of financial meltdown. The subsequent bankruptcy of General Motors was the fourth largest bankruptcy in U.S. history. Since the bankruptcy's beginning during the Bush administration, continuation during the Obama administration and carryover into the 2012 presidential election, General Motors' bankruptcy has been subject to political debate. The sheer size of the bankruptcy and the ensuing "what-if" debates makes sure that this bankruptcy will continue to be in the forefront of economic and political discussions for the unforeseeable future. Because of the importance of the GM bankruptcy, a closer look at the bankruptcy is worthwhile.

2. General Motors Company History Prior to its Bankruptcy Filing

For 77 years General Motors ("GM") was the largest auto manufacturer in the world. The brands it carries in the United States as of 2012 include Buick, Cadillac, Chevrolet and GMC. It operates in over 120 countries and manufactures vehicles in over 30 countries, employing over 200,000 people worldwide. General Motors is the largest original equipment manufacturer in the United States and the second largest in the world.

General Motors was first organized on September 15, 1908 by William Durant. Durant was first involved in the horse-drawn vehicle industry before he made a leap into the automobile industry. The first brand of automobile carried at the inception of the new company was Buick.

Durant began expanding the company rapidly in the following decades. General Motors acquired Oldsmobile Works (later known as "Oldsmobile") in 1908. In 1909, General Motors acquired Cadillac for \$55 million. General Motors acquired Oakland Motor Cars (later known as "Pontiac") the next year. In 1911, General Motors formed General Motor Trucks (later known as "GMC") from two existing companies it had previously purchased. In 1918, General Motors acquired Chevrolet. There was a deliberate philosophy behind the expansion and selection of companies to acquire – General Motors aimed to offer "a car for every purse and every purpose". The company then began to expand into acquiring companies in industries other than automobile manufacturing following the purchase of Chevrolet. In 1919, General Motors purchased Dayton Wright, an airplane manufacturer.

The company's rapid expansion did not slow entering the mid-1900s and it would continue all the way to the turn of the 21st century. General Motors would enter into multiple joint ventures, partnerships and investments in overseas companies in addition to expanding domestically. In 1943, the company acquired Yellow Truck and Coach. In 1959, General Motors would form a defense systems division which would design and develop weapons systems for the military.

By the 1960s General Motors had a 50% market share of the automobile manufacturing industry, representing the largest market share in the world, and it would only continue to expand its brands and models. Early in the 1980s it acquired Electronic Data Systems and Hughes Electronics. In 1989, it purchased 50% of Saab and would acquire the rest of Saab in 2000. In later years it also acquired major brands such as Hummer and Saturn.

The years that marked major expansion for General Motors also marked a period of a shift in consumer needs. Increased gas prices in the latter half of the 20th century created a need for smaller, more fuel efficient cars. General Motors had been continuing to emphasize production of large trucks and sport utility vehicles but would ultimately see the need to begin to adapt its business model and begin investing in energy and fuel efficiency in its vehicles.

In 1971, General Motors produced an engine that could run on no lead, or unleaded, gasoline. General Motors also produced the world's first catalytic converter in 1974. In the 1980's General

Motors entered into a strategic partnership which included Saturn and Toyota which became known as NUMMI, a joint venture focused on the production of small, fuel efficient cars. Ultimately though, the efforts of General Motors during this time period proved to be reactive to the consumer trends rather than proactive, in contrast with its Japanese and German competitors who began producing smaller and more fuel efficient cars much earlier. General Motors ultimately began to lose market share and found itself trying to find new ways to revolutionize fuel efficiency to once again regain its market share.

General Motors then turned to developing hybrid systems after the turn of the 21st century in order to capitalize on a different market. In 2005, it produced its first hybrid system which utilized a belt-alternator. The company also began developing technology for fuel cells and created the world's first fuel cell powered truck, which it introduced to the United States military service. In 2007, General Motors introduced a prototype for the Chevrolet Volt, a car model for citizens rather than the military, which utilized fuel cell technology.

Despite all of General Motors' efforts, the United States auto manufacturing industry as a whole declined following the economic trouble in the United States in the 21st century and General Motors was not sheltered from its effects. In 2008, the industry lost 50% of its sales and over 400,000 jobs [23].

A major concern of the United States and its government was the effect that a collapse of its domestic auto manufacturing industry would have on the United States economy. On November 5, 2008 the Center for Automotive Research, a Detroit-based consulting group, predicted that if one of the three major domestic auto manufacturers (Chrysler, General Motors and Ford) were to fail, the result could mean as many as 3 million jobs in the United States would be lost, taking into account the effect that such a failure could have on parts suppliers, the market and possibly the financial success of the other two manufacturers [14].

During its domestic economic crisis in 2008, the United States government enacted the Troubled Assets Relief Program ("TARP"), which set aside billions of dollars in funds to invest in failing companies in order to provide them with the capital necessary to survive hard times and become viable during a time when financing was difficult to obtain. In response to the troubles of the auto manufacturing industry the United States Government set aside TARP funds specifically for domestic bailouts of auto manufacturing companies and on December 19, 2008 the Auto Industry Financing program was

established to prop up the auto industry and its financing arms.

Despite its efforts to recapture the automobile manufacturing industry market by investing in fuel efficient cars, hybrid and fuel cell technology General Motors was still declining sharply by the end of 2008. After having a market share of as much as 50% in the 1960s and 45% in the 1980's its market share plummeted to less than 20% as of 2009[15]. It struggled to compete with foreign competitors for multiple reasons. Primarily, General Motors did not provide an affordable model line for consumers consistent enough with their needs during a time of rising oil prices. Also chief among reasons for its decline was the cost structure of General Motors' business model. Its labor was, and still is, highly unionized with the majority of its workforce being part of the United Auto Workers ("UAW").

As part of its collective bargaining agreements with the UAW General Motors takes on medical benefits and pension obligations owed to the employees and retirees of the UAW, creating massive liabilities for the company. Its foreign competitors have a much more advantageous labor-cost structure because governments in foreign countries provide medical and retirement benefits for employees in those markets, thus the responsibility of these benefits does not come from the pockets of foreign competitors. The healthcare costs that General Motors was responsible for by the end of 2008 added an additional \$1,500 to the cost of manufacturing each vehicle that it sold. General Motors also, as part of its collective bargaining agreements with the UAW, has funding obligations for an independent Voluntary Employee Beneficiary Association ("VEBA") trust which administers medical and pension benefits to retired UAW employees. These funding obligations proved extremely burdensome and unmanageable for General Motors at the end of 2008 when the company had a \$20 billion funding obligation [18].

By the end of 2008 General Motors was in such poor condition that it was widely known that the company would have to liquidate if it did not receive any assistance. The company posted a pre-tax net loss of \$30.86 billion during 2008, and in the prior year posted a pre-tax loss of \$43.297 billion. According to its balance sheet, the company had only \$91.047 billion in total assets compared to \$176.387 billion in liabilities. It had \$73.91 billion in current liabilities against only \$13.966 billion in cash and marketable securities. The condition of the company was so poor that the auditors for its 2008 annual report, Deloitte & Touche, LLP, issued a "going concern" opinion indicating the firm's belief that General Motors could not continue operations for the

foreseeable future and essentially predicting a collapse for its client [10]. There was a clear liquidity crisis for General Motors; it had incredible liabilities mounted against few assets and negative equity. It desperately needed financing but its financial condition was so dire that it was having trouble gathering credit or equity from any institution.

In 2008, the United States government realized it was imperative to make funds from the Auto Industry Financing Program available for General Motors. General Motors was, at the time, its largest domestic original equipment manufacturer in the country and employed about 91,000 persons domestically. This number does not include the thousands of people employed by the parts suppliers to whom General Motors, at the time, was making annual payments equal to about \$50 billion. There were 600 domestic automobile parts manufacturers for whom General Motors contracts made up at least 30% of revenue [15]. There is little doubt that had General Motors been forced to liquidate then these 600 suppliers would have been in dire jeopardy, and thousands of other suppliers would have lost business and been forced to downsize, the result of which would mean hundreds of thousands of jobs lost in the United States.

General Motors, unable to find financing from other sources, went before the United States government, headed by President George W. Bush, in December of 2008 to plead for assistance under the Auto Industry Financing Program, originally asking for \$18 billion in order to remain a viable company. General Motors presented a viability plan to the United States Government at this time to prove that the funds would help them remain competitive and ensuring that funds received would not go towards futile efforts. The plan called for efforts to invest in increased production of smaller, more fuel-efficient cars, a reduction in the number of its over 6,000 United States dealerships and negotiations to restructure its collective bargaining agreement with the UAW. The United States Government deemed this viability plan unsatisfactory, however, primarily because the plan did not address specific objectives on how to accomplish its proposals; it was deemed too vague.

Recognizing the necessity of propping up General Motors and providing financial assistance, the United States Treasury granted the company a Treasury Prepetition Loan anyway on December 31, 2008 for \$13.4 billion – less than the originally requested \$18 billion.

The Treasury Prepetition Loan of \$13.4 billion would be made available to General Motors in three installments: The first \$4 billion would be available

immediately, \$5.4 billion would be available in January 2009 and the remaining \$4 billion would be available February 17, 2009. There were conditions tied to the loan, as part of the terms of the loan, which required several mandated steps for General Motors to follow which the government believed would help it achieve viability. The loan specifically stated that if by March 31, 2009 (approximately 3 months after the loan was granted) a designee of the President of the United States had not issued a certification that General Motors had created a sufficient plan to take all the necessary steps to achieve long-term viability as outlined by the terms of the loan, then the entire \$13.4 billion loan would automatically become payable to the United States Treasury 30 days later [15]. Considering the massive current obligations of General Motors, its lack of liquidity and inability to obtain outside financing, not obtaining such a certification would essentially mean that the government would force General Motors into liquidation.

By the time General Motors was due for the third payment of its Treasury Prepetition Loan a new president took office for the United States, Barack Obama. Determining the certification of the viability plan General Motors would submit at the end of March 2009 would fall on the administration of this new president. On February 15, 2011 Barack Obama announced the creation of an interagency Presidential Task Force on the Auto Industry which would be designated to review the viability plan. This task force was chaired by Treasury Secretary Timothy Geithner and National Economic Council Director Lawrence Summers. The President then created the Treasury Auto Team which had the primary responsibility of helping evaluate the restructuring plan General Motors would submit as well as negotiating terms of any further assistance the United States Treasury would provide General Motors. The Treasury Auto Team was headed by Rob Bloom, a former investment banker and Steven Rattner, a cofounder of The Quadrangle Group, a private equity firm.

On February 17, 2009 General Motors submitted its new plan for viability as conditioned by the Treasury Prepetition Loan. The plan General Motors submitted called for reducing the number of plants in the United States from 47 to 32 by the year 2014 and the number of United States employees from 92,000 to 72,000 by the year 2012. The plan also called for shedding unprofitable brands carried by General Motors in the United States, specifically Saab, Hummer and Saturn. Sixteen hundred and fifty General Motors dealerships were also planned to be terminated by 2014 as part of the plan [23]. General Motors claimed that these restructuring efforts would

allow it to be a leaner company and give it the ability to invest more money into its profitable assets.

After careful review the Obama administration, with assistance in its decision from its appointed task forces, rejected the viability plan on March 30, 2009 claiming that it was not aggressive enough, failed to answer major questions and did not merit taxpayer assistance. However, rather than making the loan fully payable in 30 days from March 31, 2011, the president extended the deadline for General Motors to create an aggressive and sufficient plan by 60 days and agreed to provide General Motors with working capital as assistance which it would need to continue to operate for these 60 days, provided that General Motors was actively taking steps to create this aggressive plan. It was at this point that the President indicated his inclination that General Motors consider utilizing the United States Bankruptcy Code to accomplish this innovative plan. He indicated the need for a “fresh start.”

It was with this decision by the Obama administration that General Motors began preparing to undergo an aggressive restructuring. The company from this point forward would need to focus on negotiating with its largest creditors and create a prepackaged bankruptcy plan to quickly go through the United States bankruptcy process.

3. Details of the General Motors Restructuring Process

After the presidential task force under the direction of Barack Obama declined to certify the viability plan presented by General Motors, the company was forced to begin planning and executing an aggressive restructuring plan. The new restructuring efforts which General Motors planned to execute involved utilizing Chapter 11 of the United States Bankruptcy Code, and the process necessary to implement such a plan involved negotiating with its largest creditors in an effort to prepackage a plan of reorganization which would ensure the quickest and most efficient bankruptcy procedure possible in order to quickly reorganize and restructure the company.

The United States Government agreed to provide General Motors with working capital for 60 days while it planned and created a new restructuring plan. Because the working capital for operations would run out after this window, General Motors would have to file for Chapter 11 bankruptcy protection on June 1, 2009. Thus, General Motors would need to complete the prepackaging process by this date. The restructure that General Motors planned to execute involved leveraging subsection 363 of the United States Bankruptcy Code which allows debtors to sell their assets while undergoing bankruptcy procedures. General Motors planned to

use subsection 363 in a manner similar to companies such as Chrysler where it would sell substantially all of its assets to a purchaser, give consideration to certain of its creditors in provisions of the sale, and then confirm a liquidation plan under Chapter 11 where the consideration General Motors received from the subsection 363 sale would be distributed among the remaining creditors. The purchasing company would then become the restructured General Motors. There were two major creditors that General Motors would have to negotiate with in order to successfully prepackage a bankruptcy plan. The largest secured debt against General Motors at the time was a \$20 billion funding obligation to the UAW administered independent VEBA trust [18]. The other major creditor was general unsecured bondholders to which it had \$27.2 billion in outstanding debt [30].

The additional working capital provided by the United States Government came at two major points. On April 24, 2009 the United States Treasury extended an additional \$2 billion to General Motors as additional financing under the Treasury Prepetition Loan [13]. Then on May 20, 2009 General Motors borrowed an additional \$4 billion under the loan from the Treasury. Combined with the aid of \$13.4 billion given to General Motors on December 31, 2008 the total financing extended to General Motors by the United States Treasury was \$19.4 billion. All of the financing provided to General Motors was on a senior secured basis [15]. One of the conditions provided by the United States Government for the additional financing received was that current Chief Executive Officer of General Motors, Rick Wagoner, was forced to resign. Fritz Henderson would become the Chief Executive Officer of the company as it went through its restructuring efforts.

On May 8, 2009 General Motors announced the results of its first quarter of operations for the 2009 fiscal year. The results showed poor performance, similar to its annual report for the year 2008, and further highlighted the need for General Motors to undertake its aggressive restructuring plan. In the first quarter of 2009 General Motors showed a net loss before income taxes and equity income of \$6.061 billion. The total operating loss for the quarter was \$5.662 billion. At the end of the first quarter General Motors showed that it had only \$82.29 billion in total assets against \$172.81 billion in total liabilities. It had \$36.776 billion in current assets while having \$80.798 billion in current liabilities. General Motors' quarterly revenue had decreased by almost \$20 billion compared to the first quarter of 2008, from \$43.838 billion in the first quarter of 2008 to only \$22.431 billion in the first quarter of 2009, a total decrease of over 47%. To further highlight the

company's liquidity crisis, General Motors had a deficit in cash flows from operating activities of over \$9.39 billion in the first quarter of 2009; it had only a \$1.5 billion deficit in cash flows from operating activities in the first quarter of 2008 [11].

After the first quarter results were announced, Albert Koch of AlixPartners, LLP performed a liquidation analysis of General Motors in order to conclude how the company's assets would be distributed if it were to be forced into liquidation without restructuring and what value each of General Motors' creditors would be able to recover in the case of liquidation. The analysis considered the effects assuming that General Motors had to file for bankruptcy protection under Chapter 7 of the United States Bankruptcy Code on June 1, 2009, rather than protection under Chapter 11 where the company could restructure. The results of the analysis concluded that much more value for creditors would be recovered if General Motors was able to restructure rather than liquidate.

In the liquidation analysis, AlixPartners pointed to the fact that liquidation by General Motors would be one of the largest and most complicated in United States history and then added that it would be the largest domestic original equipment manufacturer in United States history to liquidate. There would be almost no precedent for the proceedings of the liquidation, and thus AlixPartners concluded that it could take two years before the liquidation actually concluded and distributions to creditors took place. AlixPartners also predicted that such a large liquidation would be tremendously expensive and the costs associated would be between \$2.0 and \$2.7 billion, leaving value of only about \$6.5 and \$9.7 billion to be recovered by creditors [2].

The liquidation analysis outlined in detail that only a fraction of the value for each of General Motors' assets (as listed per the balance sheet in the form 10-Q General Motors filed at the end of the first quarter of 2009) would be recovered in the liquidation. General Motors had a net book value of accounts receivable totaling \$1.3 billion, but in liquidation it was predicted that only \$500 to \$600 million of that value would be recovered. Inventory had a book value of \$3.2 billion, but the liquidation analysis predicted that only \$600 to \$900 million of this value would be recovered. Property Plant and Equipment was listed at a book value of \$18 billion which was predicted in liquidation to only yield a \$1.3 to \$2.1 billion recovery. Other Assets totaled \$4.10 billion in book value and the liquidation recovery was predicted at only \$200 to \$400 million.

The liquidation analysis broke down the many costs that would be associated with the liquidation. To liquidate under Chapter 7 of the United States

Bankruptcy Code a case trustee would need to be appointed by the bankruptcy court to manage the liquidation and oversee the distribution. This trustee would have fees equal to 1% of the total proceeds of the liquidation, according to AlixPartners. The liquidation also would require professional fiduciaries such as attorneys, accountants, brokers, liquidators and other professionals hired by both General Motors and its creditors. AlixPartners estimated the total costs of these professionals at 1.5% of the total liquidation proceeds. Wind-down costs would be another major cost category of the liquidation. These costs include those required while discontinuing the operations of the business. An example would be the cost of the corporate accountants who would need to close all of the open books of General Motors, or the engineering costs that would be incurred when valuing intellectual property in order to maximize recovery. Wind-down costs were estimated at \$1.8 to \$2.5 billion [2].

Most importantly, the liquidation analysis predicted the value that would be recovered by each group of General Motors creditors. The United States Treasury had provided General Motors with almost \$20 billion in financing and the liquidation analysis predicted that the Treasury would only be able to recover between 12% and 28% of its financing, or between \$2.6 and \$4.9 billion. Other senior secured credit which was outstanding for General Motors included a revolving credit facility and a secured term loan totaling \$5.4 billion. The estimated recovery for this senior secured debt was between \$3.1 and \$3.9 billion. There was \$116 billion in general unsecured debt held by General Motors including \$27.2 billion in general unsecured debt from general unsecured bondholders. The liquidation analysis predicted that there would be *absolutely no recovery* for these creditors [2].

The major creditors of General Motors understood the need to allow the company to reorganize in order to maximize their incremental recoveries. The UAW was very willing to negotiate with General Motors in order to reduce the \$20 billion funding obligation General Motors had to its independent VEBA trust and to also restructure its collective bargaining agreement to lower the labor cost for General Motors. These negotiations were imperative to the viability of any restructuring efforts. On May 21, 2009, after a long negotiation process, General Motors was able to reach a deal with the UAW. The deal was largely a swap of debt for equity. General Motors agreed to fund a newly established independent VEBA trust managed by the UAW after General Motors restructured. The new independent VEBA trust would take the place of the old independent VEBA trust to which General

Motors owed a \$20 billion funding obligation and the new independent VEBA trust would fund the same retiree benefits as the old independent VEBA trust. The new independent VEBA trust would be funded by three notes payable which totaled \$2.5 billion, \$6 billion worth of 9% perpetual preferred stock in the restructured General Motors, a 17.5% ownership stake in the restructured General Motors and warrants to purchase an additional 2.5%. The UAW also entered into a new collective bargaining agreement with General Motors which reduced the labor cost structure of the company [21].

After coming to terms with the UAW, the major creditor General Motors had left to strike an agreement with in order to create a prepackaged bankruptcy plan and ensure a speedy restructuring process was its general unsecured bondholders which held \$27.2 billion in general unsecured debt. Coming to terms with bondholders would be the toughest task for General Motors in its restructuring efforts because of the dilution of the ownership of bonds. Owners of General Motors unsecured bonds included both large institutional purchasers as well as individual purchasers. For the purposes of creating a prepackaged bankruptcy, General Motors would need approval from bondholders holding at least half the number of outstanding bonds and two-thirds the amount of outstanding bonds. On June 1, 2009 General Motors was due to pay \$1 billion in interest payments on its outstanding general unsecured bonds which it announced that it did not have the liquidity to actually pay [17].

Institutional bondholders making up roughly 20% of the number of the outstanding general unsecured bonds formed an ad-hoc committee which would negotiate terms of a deal with General Motors. The first deal that General Motors offered to general unsecured bondholders was a debt for equity deal in which General Motors offered bondholders a 10% equity interest in General Motors after it restructured. All general unsecured bondholders were given ballots to vote on the deal which they could mail in. Only 15% of general unsecured bondholders agreed to the original deal by ballot after the ad-hoc committee dissented and publically encouraged bondholders to not vote to agree to the deal [26].

The ad-hoc committee released public statements in which it discouraged bondholders from voting to agree to the deal:

We believe the offer to be a blatant disregard of fairness for the bondholders who have funded this company and amounts to using taxpayer money to show political favoritism of one creditor over another...Today's posturing makes it clear that the company and the auto task force

would rather discount the thousands of individual investors and retirees who own GM bonds than undergo earnest negotiations [24].

General Motors would continue to negotiate with the ad-hoc committee of bondholders and on Thursday, May 28, 2009 the committee and General Motors came to terms on an agreement which the ad-hoc committee accepted. The new deal gave bondholders a 10% ownership share of General Motors after it would restructure, as in the original deal; however, the new deal also gave bondholders warrants to purchase an additional 15% of the restructured company at a discounted price. As a condition to the deal none of the warrants bondholders received could be exercised until the value of the restructured General Motors became at least \$15 billion. Combined with the 15% of bondholders who accepted the previous deal, a total of 35% of bondholders had accepted the newly negotiated deal as of Thursday, May 28, 2009, but over 50% of bondholders were required to vote to agree to the deal by Saturday May 30, 2009 by ballot in order for the deal to be effective as a prepackaged bankruptcy plan [30]. Ultimately, 54% of bondholders making up a total of over two-thirds of the value of outstanding General Motors general unsecured bonds would vote to agree to the plan. As part of the deal, the accepting bondholders agreed not to challenge the restructuring plan during bankruptcy proceedings [25].

General unsecured bondholders would have to wait considerably longer than the UAW to receive their ownership in the restructured General Motors. The deal with bondholders was set in such a way that the 10% ownership share in the restructured General Motors and the warrants to purchase the additional equity would be given by the purchasing entity that would be restructuring as General Motors to the General Motors that would be liquidating in bankruptcy as consideration for the subsection 363 purchase of General Motors' assets. This equity would then be distributed to the bondholders after the liquidation plan was confirmed.

With agreements with the UAW and bondholders in place, General Motors officially filed a petition for bankruptcy protection on June 1, 2009, as originally planned, under Chapter 11 of the United States Bankruptcy Code with the Southern District of New York. General Motors would pursue the originally planned prepackaged bankruptcy plan of reorganization whereby its assets would be sold to a purchasing company under subsection 363 of the bankruptcy code which would restructure itself as General Motors, while the old General Motors would be left to liquidate under Chapter 11. The purchasing

entity was formed by the United States Treasury and it was officially titled Vehicle Acquisition Holdings, LLC [15]. After purchasing all of General Motors' assets, Vehicle Acquisition Holdings, LLC would change its name to General Motors Company and would represent the restructured General Motors. The General Motors Company that filed for bankruptcy and would be selling its assets to Vehicle Acquisition Holdings changed its name to Motors Liquidation Company. Motors Liquidation Company would remain in bankruptcy after the subsection 363 sale of its assets with the purpose of liquidating under Chapter 11 of the Bankruptcy Code and settling all claims against General Motors that would not be settled by the purchasing company [31]. For purposes of simplicity for the duration of this report, Motors Liquidation Company will be referred to as "Old General Motors" and Vehicle Acquisition Holdings (subsequently to be referred to as General Motors Company) will be referred to as "New General Motors".

The United States Treasury provided \$30.1 billion as financing to create New General Motors, bringing its total aid to the General Motors restructure to almost \$50 billion. The Governments of Canada and Ontario also agreed to invest a total of \$9.1 billion in New General Motors in order to help it achieve viability. This additional financing came on the condition of a speedy reorganization and required that the subsection 363 sale where New General Motors would be acquiring Old General Motors' assets was approved by the bankruptcy court in the Southern District of New York on an expedited basis by July 10, 2009. The rationale behind this need for a speedy sale was that operations were continued under the General Motors brand name during the bankruptcy proceedings and funded by Old General Motors, who no longer had the finances to keep operations sustained for a long period of time. Operations might have ceased completely for a period of time during the bankruptcy process if the purchase was not completed on a timely basis. Ultimately the subsection 363 sale would be approved and confirmed by Judge Robert E. Gerber on July 5, 2009 [15].

The New General Motors would have the following ownership structure when it completed the purchase on July 5, 2009: The United States Treasury owned 60.8% of the company, the UAW owned 17.5%, the Governments of Canada and Ontario owned 11.7%, and Old General Motors Company owned 10% (and this equity interest was reserved for distribution to general unsecured bondholders after Old General Motors confirmed a plan of liquidation) [27]. New General Motors was the only bidder in the subsection 363 sale, thus it was the winner of the sale

because there were no competing bids. As consideration for the sale, New General Motors offered the following to Old General Motors:

- i. A credit bid by the U.S. and Canadian governments of the majority of the outstanding debt held by each entity.
- ii. The assumption by New General Motors of approximately \$6.75 billion of Old General Motors' liabilities.
- iii. 10% of the post-closing outstanding shares of New General Motors (to be distributed to general unsecured bondholders).
- iv. Two warrants for the additional purchase of 7.5% equity each in New General Motors (to be distributed to general unsecured bondholders).
- v. Agreements to take on additional liabilities of Old General Motors.

Assets sold under subsection 363 of the bankruptcy code are sold free and clear of any liens or previously liability. The only liabilities that are transferred from the selling entity to the purchasing entity are those that are specifically agreed on by the purchasing entity. In the subsection 363 sale that occurred between Old General Motors and New General Motors during the Chapter 11 bankruptcy, all of the assets of Old General Motors were sold to New General Motors except for the following items:

- i. \$1.175 billion in cash or cash equivalents
- ii. Equity interest in the Saturn brand
- iii. Certain real and personal property
- iv. Bankruptcy avoidance actions
- v. Certain employee benefit plans
- vi. Certain restricted cash and cash receivables

All of the liabilities Old General Motors held before the subsection 363 sale took place would remain with Old General Motors after the subsection 363 sale. Only the following liabilities of General Motors' assets would be transferred to New General Motors as part of the purchase:

- i. Substantially all product liability claims that arise from previously purchased General Motors products *after the closing of the subsection 363 sale, regardless of when they were purchased, provided that the claims arise after the sale closes.*
- ii. All product warranty obligations of Old General Motors.
- iii. All employment related obligations for all UAW employees.

There were several liabilities that were specifically held by Old General Motors in the purchase agreement and would not be transferred to New General Motors. As part of the purchase agreement between the two entities New General Motors refused to take on these specific liabilities:

- i. Product liability claims, arising from General Motors products, which *existed prior to the subsection 363 sale of assets*.
- ii. Liabilities for claims arising from employee exposure to asbestos.
- iii. Liabilities to third parties for contract tort.
- iv. Liabilities related to any implied warranties from common law.
- v. Employment related claims not arising from UAW employees [15].

New General Motors also guaranteed offers of employment to all UAW and non-unionized employees of Old General Motors as part of the subsection 363 sale. Essentially this meant that employees that were part of non-UAW unions were not guaranteed jobs after the sale took place. New General Motors would also assume the new collective bargaining agreement with the UAW where some labor costs were cut and a new independent VEBA trust was set up to replace the old independent VEBA trust for benefits to UAW retirees. The new trust would be funded by New General Motors.

In its approval hearing, the subsection 363 sale was met with several objections by different classes and groups of claimholders against Old General Motors which Judge Robert E. Gerber had to address in his decision. The main groups who posed objections to the sale included: the F&D Bondholders Committee, an ad hoc committee of Old General Motors general unsecured bondholders which collectively held about 0.1% of its outstanding bonds; tort litigants holding outstanding product liability claims against Old General Motors; tort litigants holding outstanding asbestos exposure liability claims against Old General Motors; and non-UAW union representatives acting on behalf of their retirees who were former employees of Old General Motors.

The F&D Bondholders Committee was headed by Oliver Addison Parker. The committee and Mr. Parker argued that subsection 363 of the bankruptcy code was being utilized improperly. The committee contended that subsection 363 was not meant for selling substantially all of a debtor's assets and that the action of distributing that great a proportion of a debtor's assets should be reserved for the confirmation of a Chapter 11 plan of reorganization. The committee was contending that the subsection 363 sale represented an impermissible *sub rosa* plan – a plan of reorganization by a debtor that circumvents the conventional bankruptcy process and attempts to not adhere to the normal requirements.

The F&D Bondholders Committee also complained about the way that the purchaser only took on certain liabilities and contracts held by Old General Motors instead of all contracts, further

contending that the plan was a *sub rosa* plan. There were three contracts which the committee specifically argued [15]:

- i. The purchaser's assumption of all of the seller's contracts with suppliers
- ii. The guarantees of employment offers by the purchaser to all non-unionized and UAW personnel of Old General Motors
- iii. The purchaser's assumption of a modified collective bargaining agreement with the UAW, including the obligations to fund a new Independent VEBA trust.

Finally, the F&D Bondholders Committee contended that the nature and extent of the United States Treasury's Treasury Prepetition Loan given to Old General Motors as financing represented equity more than it did debt, and thus the funds should be re-characterized as equity for the purposes of bankruptcy proceedings. The committee concluded that the United States Treasury's claims against Old General Motors should be considered subordinate to the claims of the general unsecured bondholders because general unsecured debt receives a higher priority under United States bankruptcy law than equity. Additionally, the committee contended that because the financing given by the United States Treasury was equity, rather than debt, the Treasury had no right to credit bid as consideration for the subsection 363 sale, thus bringing the value of sale's consideration down considerably.

Tort litigants who had product liability claims and asbestos exposure claims outstanding against Old General Motors objected to the limit of successor liability granted to New General Motors when purchasing the assets of Old General Motors. The litigants contended that the purchasing entity should not be able to purchase the assets of Old General Motors without having to accept the product liability responsibilities that Old General Motors had, and thus the product liability and asbestos exposure litigants should be able to exert their claims onto New General Motors.

A committee representing the product liability litigants claimed that the wording of the bankruptcy code under subsection 363 (f) specifically permits assets to be sold free of *interests* but makes no mention of being sold free from *claims*. Further, the product liability litigants contended subsection 1114 (c) of the bankruptcy code provides evidence that Congress specifically wished to exclude claims from subsection 363 (f). Subsection 1141 (f) of the United States Bankruptcy Code outlines regulations for property distributed in a Chapter 11 plan confirmation and both the words *interests* and *claims* are specifically used in that subsection. Subsection 1141 (c) states "property dealt with by the plan is free

and clear of all *claims and interests... in the debtor*" [15 p.55]. The committee of product liability litigants contended that because Congress specifically chose to include the terms *interest and claims* in a subsection addressing property distributed after confirming a Chapter 11 plan, but specifically excluded the word *claims* in subsection 363 (f), it should be interpreted that Congress did not intend for property sold in a subsection 363 sale to be sold free of claims, only interests. Thus successor liability should not be limited on the assets New General Motors purchased from Old General Motors and New General Motors should be responsible for the claims of the product liability and asbestos exposure litigants.

Committees which represented the retirees of three different non-UAW unions presented objections to the subsection 363 sale. These non-UAW unions objected to provisions of the sale which stated that New General Motors would not be taking on the obligations that Old General Motors owed to their retirees. These committees all submitted affidavits from their retirees describing how difficult it is for their retirees to get by without their entitled medical benefits and how some who do not qualify for Medicare have no medical insurance if it is not provided by New General Motors. These unions based their case on regulations mandated in subsection 1114 of the United States Bankruptcy Code which outline a process that debtors in possession must adhere to before they are allowed to either modify or neglect retiree benefits. The regulations in subsection 1114 call for a debtor to gain approval from a bankruptcy court before modifications or lack of payment of retiree benefits can occur, and before the debtor can go before a court for approval the debtor must negotiate in good faith with a committee representing the retirees to try and compromise on reduced benefits which are acceptable for both parties. The committees contended that both Old General Motors and New General Motors did not first confer or negotiate with these non-UAW union retirees before Old General Motors sent a notification to each of these unions explaining that their retiree benefits would no longer be honored.

There were also smaller objections to the subsection 363 sale of assets from less prominent objectors. Most notable were objections from environmental advocates that New General Motors would not be bound to environmental clean-up responsibilities which Old General Motors had. The most notable among the environmental advocates was the Attorney General of the State of New York. Similar to the claims of the product liability and asbestos exposure litigants, the arguments of the

environmental advocates rested under the theory of successor liability; that the claims against the assets of Old General Motors should be carried to New General Motors. These environmental advocates were also concerned with whether New General Motors was going to be required to comply with environmental law after purchasing the assets from Old General Motors.

Judge Robert E. Gerber ruled against all objections and approved the subsection 363 sale of Old General Motors' assets to New General Motors on July 5, 2009. After New General Motors acquired Old General Motors' assets, New General Motors became the restructured General Motors. Old General Motors remained a debtor in bankruptcy and continued the Chapter 11 bankruptcy proceedings for the next two years pursuing a plan of liquidation. On March 18, 2011 Old General Motors (Motors Liquidation Company) filed its Second Amended Joint Chapter 11 Plan. That plan was approved on March 29, 2011 and became effective on March 31, 2011. After the liquidating plan became effective, general unsecured bondholders became entitled to the equity which they had agreed upon in the prepackaged bankruptcy plan. The securities which general unsecured bondholders previously held were terminated on March 31, 2011. On April 21, 2011 general unsecured bondholders received their initial distribution of New General Motors stock (which by that time had already gone public) [31].

There were different classes of general unsecured bonds outstanding against Old General Motors, each with different interest rates and maturity dates. Depending on the type of bond held, general unsecured bondholders received a distribution of up to 4 shares of New General Motors Stock per every \$1,000 dollars of bonds they held. Stock in New General Motors was trading publically at a high of \$31 dollar per share on the day of distribution [32]. Depending on the number of shares of common stock distributed to a particular bondholder, bondholders received a maximum value of up to \$124 per \$1,000 of bonds they held, plus the value of warrants that the bondholders received. Two types of warrants were distributed to unsecured bondholders and up to 4 warrants of each type per \$1,000 of bonds held were distributed, depending again on the type of bond a particular bondholder had. Class A Warrants gave bondholders the right to purchase New General Motors stock at \$10 per share and Class B warrants gave bondholders the right to purchase New General Motors stock at \$18.33 per share [16].

4. General Motors Post Restructure

After the subsection 363 sale was executed, New General Motors changed its name from “Vehicle Acquisition Holdings” to “General Motors Company” (subsequently in this section, New General Motors will be referred to as “General Motors”). After completing its restructuring efforts the company would reemerge with only four of its most profitable major brands in North America: Buick, GMC, Chevrolet and Cadillac. The other brands it carried in North America were either sold or wound down. In 2009, General Motors decided to wind down its Saturn and Pontiac brands. In 2010, General Motors sold its Saab brand to Spyker Cars. Also in 2010, General Motors had agreed to an initial sale of its Hummer brand, but the sale was eventually rejected and unsuccessful, resulting in a wind down of Hummer’s operations.

General Motors emerged from the subsection 363 sale of assets a much leaner company with a much more competitive cost structure. It cut its workforce by over 20% from the end of the 2008 fiscal year to the end of the 2009 fiscal year. General Motors also reduced its number of manufacturing plants. It had 47 manufacturing plants at the end of the first quarter of 2009 before the company filed for Chapter 11 bankruptcy protection, but after coming out of Chapter 11 through the subsection 363 sale it planned to reduce that number to 33 plants by the end of 2012. General Motors also planned to cut its North American dealership network. There were over 6,000 General Motors dealerships before it filed for Chapter 11 protection, but the company, after restructuring, planned to eventually reduce that number to only 4,100 dealerships. With its new cost structure General Motors would have a breakeven point at 10 million new car sales. Before bankruptcy proceedings General Motors’ breakeven point was over 16 million new car sales. Initially, the restructuring efforts were a success and General Motors was able to earn \$4.2 billion in the first nine months of its initial year after emerging from the subsection 363 sale [7].

In 2010, General Motors began preparing to go public and on November 17, 2010 held its initial public offering. It was one of the largest in United States history. It sold 478 million shares of common stock at \$33 each, raising over \$15.7 billion in equity. General Motors also sold \$4.35 billion in preferred shares. After selling its common stock investment in the initial public offering, the United States Treasury’s share in General Motors dropped from just under 61% to under 33% [3]. The Treasury ended up selling its shares in the initial public offering for less than it effectively purchased them for originally, however. Considering the Treasury’s financing for the company, it effectively purchased

its 60.8% equity in the company for \$43.84 per share, therefore losing \$4.5 billion on its investment in the initial public offering [26]. In order for the Treasury to break even on its investment, General Motors’ share price would have to rise to \$48.58 per share, which would bring the total value of the company to a level never before attained even before restructuring [3]. After selling shares during the initial public offering the Treasury pledged not to sell additional shares for at least 6 additional months. After that time period, the Treasury stated its intent to gradually scale back its investment in General Motors.

General Motors has since kept up its solid post-restructuring performance. In its 2011 annual report General Motors reported that its income before income taxes and equity income was \$5.895 billion and its total net income was \$9.287 billion. In the 2011 annual report the company posted total revenues of \$150.276 billion and revenues from automotive sales of \$148.866 billion [9]. The balance sheet in the 2011 annual report showed that the company was in much better financial standing than it was when it released its 2009 first quarter form 10-Q. General Motors showed \$60.287 billion in current assets and \$144.603 billion in total assets in its 2011 annual report, against only \$40.932 billion in current liabilities and \$105.612 billion in total liabilities. The liquidity of General Motors was also much improved and in the 2011 annual report General Motors reported that it had gained \$8.166 billion in positive cash flows from operating activities, \$7.429 billion of which was from automotive activities. After filing for bankruptcy protection only 3 years earlier, General Motors had a credit rating from Standard & Poor of BB+ as of March 27, 2012, signaling regained confidence in General Motors debt [5]. Since then, GM has returned to profitability and the leaner GM is forecasting profitability into the foreseeable future.

5. Conclusion

The bankruptcy of General Motors and its fallout continues to be debated economically and politically. It became an issue for the presidential election of 2012 with both sides debating the merits and process. It continues to be in the news as lawsuits from closed dealerships and environmental issues wind their way through the courts. Old GM continues while new GM produces cars. General Motors, from its very beginning has been an interesting and important company to the United States.

This paper highlights the consequences a major bankruptcy has on stakeholders, especially those who may not even know they are at risk. Often, the

effects of bankruptcy are explored on large institutional investors or individuals who intentionally purchase the entity's common stock or general unsecured bonds or on the markets in general. But, the bankruptcy of General Motors emphasizes that the public's risk from a major bankruptcy goes far beyond these investors. Many stakeholders are affected by a company's bankruptcy without even knowingly taking the risk of a company's financial performance. Litigants in product liability suits against a bankrupt company, hurt through no fault of their own actions, may not be able to receive compensation for their damages as a result of a company going bankrupt. Consumers, who should be focused on vendor product quality and price rather than vendor financial performance, may not be able to exercise products rights (such as warranties or returns) if their vendor declares bankruptcy.

This paper focuses on the effects the General Motors bankruptcy, one of the largest in the history of the United States, had on stakeholders who took no calculated risk before becoming a stakeholder in General Motors. It highlights the effects the bankruptcy had on General Motors suppliers, dealership owners, employees, consumers and product liability litigants. The paper also discloses the investment effects of the General Motors bankruptcy, which in this particular case affected every American taxpayer. This paper is important because it puts into perspective just how detrimental major bankruptcies can be and who can be adversely affected.

Hopefully, the old saying "As General Motors Goes So Goes the Nation" is no longer true with regards to their bankruptcy and financial bailout.

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Authors Biographies



Christopher Bosco -Chris has been an Audit Analyst supporting asset management functions for Fidelity Investments since June, 2012. Prior to joining Fidelity, Chris spent one year as an Audit Intern at Caron & Bletzer, PLLC., a public accounting firm located in Kingston, NH, specializing in audits of employee defined benefit and defined contribution retirement plans. Chris also has experience with the Liberty Mutual Insurance Group as a Group Medical Underwriting Intern. Chris holds a BS from the University of New Hampshire and will be studying for his MS in Accounting from the University of Connecticut.



Catherine Plante, PhD, CPA – Catherine is an Associate Professor of accounting at the University of New Hampshire. She teaches Governmental Accounting and Financial Accounting at both the graduate and undergraduate level. Her current research interests include the interaction of governments' financial decisions with taxpayers and other stakeholders. Previously she was a healthcare consultant with Price Waterhouse. She received her Ph.D. in accounting from The Ohio State University.