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## Survival of the Fittest? Financial and Economic Distress and Restructuring Outcomes in Chapter 11

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University of Utah - Department of Finance

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### Abstract


We use a simple proxy to distinguish between financial and economic distress and show that Chapter 11 outcomes and asset restructurings vary systematically across these firm types. The results from our sample of large bankruptcies from 1991 to 2004 are consistent with the view that the Chapter 11 process preserves the going concern value of financially distressed firms while redeploying the assets of economically distressed firms. These results hold for asset redeployments resulting both from liquidations or acquisitions and those resulting from partial asset liquidations of firms that reorganize in Chapter 11. The empirical findings run counter to concerns that inefficiencies and conflicts of interest severely compromise the Chapter 11 process. Further, we provide the first empirical evidence that the put option inherent in lease contracts is frequently exercised in Chapter 11, that the disposition of lease contracts in bankruptcy constitutes a large portion of asset restructurings, and that the ability to put lease contracts may mitigate the indirect costs of asset fire sales. We also find that unionized firms experience smaller job losses and debt reductions in Chapter 11 than do non-unionized firms.

**Keywords:** Bankruptcy, Chapter 11, financial distress, leases, unionization, asset sales, restructuring, liquidation

**JEL Classification:** G33

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