Mega Company

Turnaround of the Year

Eastman Kodak Company / Kodak Alaris Holdings Ltd.

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During the 20th century, Kodak had been one of the most-recognized names in the world. At its peak, the company employed more than 144,000, but by year-end 2011, after years of decline in its core film business, Kodak was already a much smaller company, with 17,000 employees, annual sales of $6 billion, $4.7 billion in assets, and over $7 billion in liabilities. At the time of its Chapter 11 filing, on January 19, 2012, Kodak's business encompassed a broad portfolio of consumer and commercial products and services, and considerable intellectual-property assets.

For years, Kodak had faced a secular decline in its iconic film business brought on initially by the rise in digital cameras and exacerbated further by the proliferation of digital-image technology employed in mobile phones and tablets, resulting in reduced revenues and profitability. The company's own expansion into digital technologies required significant investment to reach scale and profitability. Kodak also had significant pension and other post-employment benefit (OPEB) obligations to employees and retirees (who outnumbered active employees by more than three to one). Certain of these pension funds, most notably in the UK, were severely underfunded.

For a number of years, Kodak had been supplementing its operational cash flows with successful patent licensing, supported by active infringement litigation, but even this source of cash flow became constrained due to unfavorable legal rulings and aggressive tactics by larger and well-capitalized defendants. When the company filed for bankruptcy, the strategic objectives for the restructuring were: (i) to bolster liquidity, (ii) to focus on the company's core business lines, (iii) to monetize non-strategic intellectual property, and (iv) to resolve legacy liabilities fairly. The bottom-line objective was to enable Kodak to make significant progress toward becoming a sustainable, profitable business, and to secure the support of creditors for its plan of reorganization and eventual emergence from bankruptcy.

The Kodak turnaround team successfully obtained $950 million of initial debtor-in-possession (DIP) financing for the company upon its filing, and quickly began to execute a global turnaround of the business. In rapid succession, money-losing and non-core businesses and assets were exited or divested, including Kodak Gallery, the company's online photo-sharing and -storage unit; new strategies and cost reduction actions were implemented for remaining businesses; additional capital was raised; and liabilities were resolved.

The turnaround professionals, working hand-in-hand with Kodak:

• In total, Kodak reduced its legacy liabilities by approximately $3 billion.

• Reached a consensual settlement agreement with the committee of U.S. retirees in October 2012 to permanently eliminate $1.2 billion in OPEB liabilities, which had hampered the company with annual cash costs of $110 million.

• Sold Kodak's digital-imaging patent portfolio in a complex, highly structured transaction to a consortium of buyers for $527 million.

• Refinanced the company's initial DIP facility in March 2013 with a new $848 million DIP term loan provided by certain second-lien lenders, which also provided for the option to convert up to $654 million of the new DIP loans into 5-year exit financing.

• Led extensive operational-restructuring and profitability-enhancement work, resulting in an annual EBITDA improvement of over $300 million, including the rejection/renegotiation of a large number of unprofitable contracts and leases, the wind-down of unprofitable and non-core businesses, significant consolidation of remaining business lines, and streamlining of corporate and R&D function.

• Developed a long-range business plan, built a "clean-sheet design" for corporate-overhead functions and R&D resources for the smaller, reorganized company, and reduced global headcount by 29 percent through emergence.

• Reached a settlement with New York State related to pre-petition environmental liabilities in June 2013, funded with a $49 million trust.

• Conducted a successful $406 million equity-rights offering to unsecured creditors under the company's plan of reorganization, and raised approximately $900 million in exit financing to fund remaining cash needs associated with the company’s emergence. The outcome of the above efforts allowed for the full repayment of the initial and refinanced DIP-financing facilities, and full repayment of remaining prepetition, second-lien notes, which had traded as low as 60 cents on the dollar in 2012.

• Commenced a sale process for the company’s consumer (Personalized Imaging) and scanner (Document Imaging) businesses in the fall of 2012, and ultimately negotiated an extraordinary, win-win settlement with Kodak’s UK Pension Plan (KPP) in April 2013, resulting in a spin-off of those businesses to the KKP in exchange for the release of all of the company’s worldwide obligations to the KPP (including the waiver of its $2.8 billion bankruptcy claim) and a $325 million cash payment from the KPP to Kodak, as further described below. Working together, Kodak, the KPP, and their turnaround teams overcame a host of seemingly insurmountable hurdles to finalize this settlement in a matter of weeks.

The first set of challenges around the KPP settlement transaction involved obtaining US bankruptcy and UK regulatory approval. Kodak and the KPP were operating under an extremely tight timetable, leaving no room for a months-long auction process. The parties, assisted by the Official Committee of Unsecured Creditors, convinced the US Bankruptcy Court that Kodak's sale to the KPP was the only viable path to emergence and would result in a value that could not be matched by any other potential bidder.

Persuading the U.K. Pensions Regulator was perhaps an even more daunting task. Rather than receive cash for its claim, the KPP would pay $325 million in plan assets to Kodak and receive in return businesses that it would have to own and operate to obtain recovery. The KPP secured approval by demonstrating that those businesses were stable, cash-producing assets that would generate higher benefits to the pensioners than any other alternative. Thereafter, to obtain member approvals, the KPP and its advisors undertook a town-hall-style roadshow across the UK, explaining the transaction and ultimately receiving overwhelming pensioner support (through votes on behalf of greater than 95% of the liabilities).

Even after the deal was approved, the parties faced a second set of challenges. To start, the KPP had never run a business before. It needed to rely on a team of advisors in 33 countries to develop and execute an operation plan for the businesses, now known as Kodak Alaris. Equally challenging, the businesses had been fully integrated with the rest of Kodak for decades, raising a host of issues on how to separate employees, operations, finances, and intellectual property.

In the end, the transaction created extraordinary value. It avoided Kodak's liquidation, avoided the UK’s Pension Protection Fund for those KPP members voting in favor, preserved thousands of jobs, and created two profitable businesses: a reorganized Kodak, owned by U.S. creditors, and Kodak Alaris, owned by the KPP. It stands as one of the most innovative, unusual, and successful deals ever consummated in the history of cross-border insolvency.

The reorganized Kodak emerged on September 3, 2013, with a right-sized capital structure and an annuity-based business model that well-positions the company to be a long-term leader in the commercial-imaging industry. Kodak's operational EBITDA improved by over $375 million from 2012 to 2013, from a loss of $215 million in 2012 to a positive $160 million in 2013. The company subsequently re-listed on the New York Stock Exchange on January 8, 2014.