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Blockbuster files for Chapter 11 bankruptcy, sets plan to reorganize

September 23, 2010

After struggling with nearly $1 billion in debt and growing competition from Redbox and Netflix, Blockbuster Inc. filed for Chapter 11 bankruptcy protection on Thursday.

The filing, long expected, would wipe out the debt and equity of the once dominant DVD rental chain and put the owners of its senior secured bonds, including activist investor Carl Icahn, in control.

Blockbuster's stores, kiosks and online services will remain in operation during bankruptcy, which will likely last only a few months if the process goes smoothly under the plan filed in U.S. Bankruptcy Court in New York.

Blockbuster executives told the major Hollywood studios in August that they expected to shutter 500 to 800 of its 3,425 U.S. stores as part of a bankruptcy process that would begin in September.

In a statement Thursday, the company only said it would "evaluate its U.S. store portfolio with a view toward enhancing the overall profitability of its store operations." Blockbuster also said that foreign operations will continue at stores in Canada, Denmark, Italy, Mexico and Britain but that it would no longer support its money-losing subsidiary in Argentina.

Going forward, Blockbuster is expected to focus more on its kiosks and digital initiatives to succeed in a rapidly changing market for movie rentals.

Icahn, a longtime media investor who is currently the largest shareholder in Lions Gate Entertainment, has been buying up Blockbuster bonds recently and is said by people familiar with the situation to own at least one-third of its total secured debt. The reorganization plan calls for him to select two of seven members of the company's board of directors once it exits bankruptcy. In addition, he and investment firm Monarch Alternative Capital will select another member jointly.

Chief Executive Jim Keyes is expected to remain in his post, one person close to the situation said.

Although the holders of Blockbuster's about $630 million in senior secured bonds will take over the company, the owners of its $300 million in unsecured debt will be wiped out, as will those who own its virtually worthless stock, which closed Wednesday at 6 cents per share.

The senior bond owners also will provide Blockbuster with up to $125 million in so-called "debtor-in-possesion" financing to continue operations during Chapter 11. The company will have access to a credit facility of up to $50 million upon exiting Chapter 11 to restart its business. Money drawn from that financing will be the company's only remaining debt under the plan.

It's unclear how Blockbuster's other debt, accumulated as part of ongoing business recently, will be treated. A filing said the company's total debt was $1.465 billion, and its assets were just over $1 billion.

Among the largest creditors that have claims against Blockbuster are the major studios. According to a court filing, the company currently owes $21.6 million to 20th Century Fox, $20 million to Warner Bros., $13.3 million to Sony Pictures, $8.6 million to Walt Disney Studios, $8.3 million to Universal Studios, and $7.9 million to Lions Gate.

Most studios are believed to be supportive of Blockbuster's efforts, as they want to see it remain in business as a viable competitor to Netflix and Redbox, particularly since Movie Gallery Inc. -- parent company of Hollywood Video, formerly the second-largest DVD rental store -- went out of business in April.

In a statement, Keyes said, "The recapitalized Blockbuster will move forward better able to leverage its strong strategic position, including a <u>well-established brand name</u>, an exceptional library of more than 125,000 titles, and our <u>position</u> as the only operator that provides access across <u>multiple delivery channels</u> -- stores, kiosks, by-mail and digital."

-- Ben Fritz, Tribune Newspapers

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