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What's next in an essential brand's Chapter 11 bankruptcy

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When a company files for Chapter 11 bankruptcy, its customers still have some hope, but once a liquidation happens things become bleak.

In any bankruptcy filing, rank-and-file customers generally stand at the back of the line.

Banks and other secured creditors are the priority, and if there's any chance of a successful reorganization, vendors also have to be taken care of.

During the Chapter 11 process, however, customers generally have some protections. Return policies are usually honored as are warranties and, sometimes, gift cards. Once a company makes the decision to liquidate, however, all bets are off when it comes to customer protections.

Regular customers generally get nothing in a liquidation, and that can include goods or services they have already paid for. For example, the recent liquidation of Mitchell Gold + Bob Williams left thousands of furniture orders stranded at various delivery companies.

The defunct chain's customers had paid for delivery, but the company had not paid its delivery partners. That led the bankruptcy court to make a deal where consumers were allowed to pay a second time for delivery if they wanted to receive their goods.

That's not a fair solution, but it's about the best consumers can expect in a liquidation. SmileDirectClub, ([SDC](#)) - [Get Free Report](#) an online company that sold teeth aligners, an alternative to braces, has moved from a Chapter 11 reorganization to a liquidation and that's very bad news for its customers.

[John Sparacino](#), a principal with [McKool Smith's Bankruptcy Litigation](#) practice area, recently answered some questions from TheStreet to explain what SmileDirectClub customers can expect.

SmileDirectClub abruptly shut down

TheStreet: Is there any chance of someone buying the assets and restarting the company?

John Sparacino: I am not involved in the case, but from news coverage reporting on counsel statements made in court, it appears that the debtors do not believe that there is any potential buyer/transaction. Based upon what has been reported, I strongly believe that there is virtually no chance of a sale and continuation of the business.

TheStreet: Are existing customers going to be forced to find other providers?

Sparacino: Yes. SmileDirect has made clear that it is ceasing its business operations and will no longer provide products or services to customers.

TheStreet: Will people who paid the company for product that has not shipped have any chance of recovering any money?

Sparacino: Highly unlikely. The customers are general unsecured creditors and are behind secured claims. There appears to be no possibility of a recovery to general unsecured creditors.

SmileDirectClub dropped its warranty

TheStreet: Would a new company buying the assets be free of any warranty promises?

Sparacino: This would really be a contractual matter (and business decision) for a buyer. Under the law, the buyer certainly can purchase free and clear of warranty obligations. However, if a buyer was interested in buying the business as a going concern, then an important business consideration would likely be maintaining (happy/satisfied) customers.

It is not uncommon for acquirers of consumer-driven businesses to adopt and assume customer obligations and customer benefit programs of the seller so as to maintain (acquire) a satisfied customer base.

A purchase agreement will delineate which seller liabilities are to be assumed by the purchaser. If the purchaser chooses to assume no such liabilities, then the bankruptcy sale would be free and clear of warranty liabilities.

TheStreet: Is there anything I'm missing from a consumer point of view?

Sparacino: No. Basically, the situation seems terribly bleak for SmileDirect customers in that there will be no further delivery of products or services, and any money paid to SmileDirect in the form of prepaids, deposits, or advances will almost certainly be lost.