RECENT RETAILER-DEBTORS CITE SUPPLY CHAIN CRISIS AS TRIGGER FOR BANKRUPTCY FILINGS

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In the aftermath of the decadelong "retail apocalypse" and onslaught of retail bankruptcy filings, 2022 saw a significant drop in retail Chapter 11 bankruptcy filings. As of November 2022, only seven large retailers had filed for bankruptcy protection[1]—a steep drop from the 52 retail bankruptcies filed in 2020 and the 21 filed in 2021. In fact, in the first half of 2022, the U.S. saw the lowest number of retail bankruptcies in the last 12 years. Despite this record low, current economic conditions may trigger a new wave of retailer filings in 2023, with supply chain issues taking center stage.

Notably, 2022 retailer-debtors do not have extensive brick-and-mortar store footprints like those that predicated many of the retailer filings in 2020 and earlier years. The more recent retailer-debtors largely cited supply chain challenges as the trigger for their bankruptcy filings. To provide an outlook on how supply chain challenges might further affect the retail industry in 2023, this article analyzes retailer distress and discusses the supply chain crisis that became the catalyst for a majority of 2022 retail filings.

Demonstrative Retail Bankruptcy Filings

An analysis of the reasons cited for four 2022 retail bankruptcies—Revlon Inc., NewAge Inc., Enjoy Technology Inc., and Packable Holdings LLC—demonstrates the effects of supply chain challenges on the U.S. retail sector.

Revlon Inc. Revlon and its affiliated debtors manufacture and sell cosmetics through the company's own e-commerce channels and through wholesale relationships with traditional retailers.[2] The Revlon Chapter 11 case serves as the prime example of supply chain issues triggering a bankruptcy filing. Revlon's CRO cited the company's heavy debt load and supply chain issues as the predominant reasons for the bankruptcy filing, in addition to tightening liquidity markets and the rapid rise of inflation.[3]

Revlon first felt the effects of supply chain challenges in 2020, but these issues became critical by the spring of 2022, particularly among suppliers of raw materials needed for the company's products.[4] Supply chain disruptions prevented Revlon from producing sufficient product to meet consumer demand, which surged following an easing of COVID-19 restrictions globally. Revlon estimates that it was unable to timely fulfill about one-third of customer demand for its products.[5]

The resulting lack of inventory had corollary effects of increasing Revlon's costs and limiting the company's access to its asset-based revolving

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Cumulatively, these factors have caused significant delays in the manufacturing and shipment of inventory, resulting in surpluses of out-of-season inventory in the hands of retailers. Adding fuel to the surplus fire, many retailers have reported that they over-ordered inventory in an effort to hedge against the supply chain crisis.

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credit facility, which was critical to maintaining sufficient access to liquidity to support the company's manufacturing operations.[6] Prepetition, Revlon's financial position weakened, and competition for raw materials and product from its vendors increased.

Cumulatively, supply chain shortages caused the costs of raw materials and shipping to increase substantially. Revlon stated that in early 2022, the time it took to ship components from China to the United States nearly doubled, and the cost quadrupled.[7] With the rapid rise in inflation globally, Revlon was unable to pass the increased costs through to its customers.[8]

As the company became unable to make timely payments for raw materials, suppliers reduced or eliminated Revlon's trade credit, accelerated payment terms, or shifted their business altogether to more liquid customers.[9] Cumulatively, supply chain issues triggered a domino effect that resulted in Revlon's inability to manufacture sufficient product and wholesaler-imposed fines for failure to deliver inventory in full and on time.

NewAge Inc. NewAge Inc. and its affiliated debtors develop, sell, and distribute health and nutritional products globally through an e-commerce, distribution, and direct-to-consumer sales network of over 400,000 brand partners. The NewAge debtors, which have no brick-and-mortar locations, filed for Chapter 11 bankruptcy protection in 2022, due in part to supply chain disruptions.[10]

The NewAge debtors' businesses depend heavily on efficient supply chains to produce and deliver products to customers throughout the world. Supply chain disruptions caused by the COVID-19 pandemic contributed to the challenges that predicated the need for bankruptcy relief when combined with uncertainty related to business operations in China, issues in fully integrating brands, changes in management, and expenses related to an investigation of a potential violation of the Foreign Corrupt Practices Act.[11]

Enjoy Technology Inc. Enjoy Technology Inc. is a mobile technology retailer that offers "e-commerce at home" through personalized in-home retail experiences.[12] Like the other filings analyzed here, Enjoy has no physical stores. Enjoy filed for Chapter 11 bankruptcy protection, citing supply chain complications as a catalyst for its financial distress. Supply chain disruptions resulted in slumping sales, which exacerbated debt load issues.[13]

Packable Holdings LLC. Packable Holdings and its affiliated debtors are U.S.-based third-party retailers that provide integrated logistics, supply chain and inventory management, data analytics, and marketing services to brand partners.[14] Packable operates across numerous online marketplaces and direct-to-consumer websites, selling health and beauty, hair care, nutrition, household, and over-the-counter medicines and medical products, among other goods. It has no physical store locations.[15]

Packable's business model was dependent on its purchase of inventory from brand partners to fulfill consumer orders placed on marketplace and direct-to-consumer sites operated on behalf of its brand partners.[16] Packable indicated that it faced increased operating expenses passed on to it from increases in the cost of goods sold from brand partners.[17] Through its Chapter 11 case, Packable is liquidating its assets and ceasing all operations.[18]

Fallout Continues

At the beginning of 2022, retailers continued to benefit from government stimulus funds they had received in 2020 and 2021. In stark contrast to the wave of brick-and-mortar retail bankruptcies in earlier years, nearly all 2022 retail-debtors sold products exclusively via e-commerce or brand partner retailers.[19] Without high overhead costs linked to rent and labor to bog down balance sheets, 2022 retail bankruptcy filings highlighted the macroeconomic and geopolitical factors that have created yet another storm for retailers.

Ever-evolving supply chain challenges, resulting from the Russia-Ukraine war and COVID-19 lockdowns in Asia, have reached critical levels. International labor shortages, which started in 2020, have persisted, keeping wages high and causing distribution, inventory, and operational problems for suppliers. In addition, elevated gas prices caused financial strain and delay earlier in 2022, which have continued into this year.

Cumulatively, these factors have caused significant delays in the manufacturing and shipment of inventory, resulting in surpluses of out-of-season inventory in the hands of retailers. Adding fuel to the surplus fire, many retailers have reported that they over-ordered inventory in an effort to hedge against the supply chain crisis. The authors anticipate that this new

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development in the supply chain crisis will be a contributing factor in retail challenges that will continue in 2023.

U.S. consumer behavior continues to evolve, leaving the retail industry to adapt. At the beginning of 2022, U.S. consumer debt rose significantly as consumers continued to buy goods. This contributed in large part to the lowest number of retail bankruptcy filings in more than a decade during the first half of the year. However, the increase in spending reduced consumers' personal savings, which have further dwindled due to stock market volatility. The second half of 2022 saw consumers curtailing their discretionary spending habits to meet their debt payments.

Due to a glut of inventory, retailers have been forced to sell their excess or out-of-season inventory at discounted prices to make room for new inventory. These discounts, which have benefited consumers, have eroded retailer profit margins and added substantial strain to their liquidity positions.

[1] Of these seven filings: one debtor had assets and liabilities of $1 billion+ (Revlon Inc.), four debtors had assets in the $100 million-$500 million range (NewAge Inc., Packable Holdings LLC, Cherryman Industries Inc., and Enjoy Technology Inc.), and two debtors had assets in the $1 million-$100 million range (Corsicana Bedding LLC and Olympia Sports Acquisitions LLC). See *In re Revlon, Inc., et al.,* No. 22-10760 [Docket No. 1] (Bankr. S.D.N.Y. filed June 15, 2022); *In re NewAge, Inc.,* No. 22-10819 [Docket No. 1] (Bankr. D. Del. filed Aug. 30, 2022); *In re Packable Holdings, LLC,* No. 22-10797 [Docket No. 1] (Bankr. D. Del. filed Aug. 28, 2022); *In re Cherry Man Indus., Inc.,* No. 22-11471 [Docket No. 1] (Bankr. C.D. Cal. filed Mar. 17, 2022); *In re Enjoy Tech., Inc.,* No. 22-10580 [Docket No. 1] (Bankr. D. Del. filed June 30, 2022); *In re Corsicana Bedding, LLC,* No. 22-90016 [Docket No. 1] (Bankr. N.D. Tex. filed June 25, 2022); and *In re Olympia Sports Acquisitions, LLC,* No. 22-10853 [Docket No. 1] (Bankr. D. Del filed Sept. 11, 2022). There were also three small retail bankruptcies filed in 2022 (Escada US (SubV), CFX US Co. Inc. (SubV), and BHCosmetics), but these companies filed to liquidate and therefore are not part of the analysis covered in this article.

[2] Declaration of Robert M. Caruso, Chief Restructuring Officer, (I) In Support of First day Motions and (II) Pursuant to Local Bankruptcy Rule 1007-2 at 19, *In re Revlon, Inc., et al.,* No. 22-10760 (Bankr. S.D.N.Y. Jun. 16, 2022), ECF No. 30.

[3] *Id.* at 4-5.

[4] *Id.* at 46.

[5] *Id.* at 82.

[6] *Id.* at 4, 8–9.

[7] *Id.* at 81.

[8] *Id.* at 9.

[9] Declaration of Robert M. Caruso, *supra* note 4, at 8.

[10] Declaration of Lawrence Perkins as Chief Restructuring Officer of the Debtors in Support of the Debtors' Chapter 11 Petitions and Requests for First Day Relief at 3, *In re NewAge, Inc.,* No. 22-10819 (Bankr. D. Del. Aug. 31, 2022), ECF No. 12.

[11] *Id.* at 3.

[12] Debtors' Combined Disclosure Statement and Chapter 11 Plan of Liquidation at 23, *In re Enjoy Tech., Inc.,* No. 22-10580 (Bankr. D. Del. Oct. 27, 2022), ECF No. 544.

[13] *Id.*

[14] Declaration of Brian Teets in Support of the Chapter 11 Petitions and First Day Motions at 3, *In re Packable Holdings, LLC,* No. 22-10797 (Bankr. D. Del. Aug. 29, 2022) ECF No. 13.

[15] *Id.* at 5-6.

[16] *Id.* at 6.

[17] See id. at 17 ("The combined strain of these factors accelerated Packable's cash burn and gave rise to a liquidity shortage.").

[18] See *id.* at 13.

[19] Olympia Sports Acquisitions LLC and its affiliated debtors, which operated 35 brick-and-mortar stores, are the outliers. Following the failed launch of its e-commerce business, Olympia Sports Acquisitions LLC and its affiliated debtors filed Chapter 11 to liquidate their businesses. See Declaration of Mark Coffey, CEO of Olympia Sports Acquisitions, LLC, in Support of First Day Motions, *In re Olympia Sports Acquisitions, LLC,* No. 22-10853 (Bankr. D. Del. Sept. 19, 2022) ECF No. 12.