NEW YORK CITY BAR

COMMITTEE ON BANKRUPTCY AND CORPORATE REORGANIZATION

CORPORATE BANKRUPTCIES: TRENDS IN ASSET SALES AND LIQUIDATIONS[1]

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1. INTRODUCTION

The global credit crisis that emerged by late 2007 after the collapse of the sub-prime mortgage markets brought to an end the sustained drought in corporate defaults and U.S. bankruptcy filings. Gone with the era of easy credit was the ability of corporate borrowers to paper over their potential defaults and maintain liquidity. The crisis quickly and dramatically engulfed nearly all asset classes, and cast doubt on collateral values as capital markets seized around the world. These market events have given rise to a steady and growing stream of U.S. chapter 11 bankruptcy filings. This note considers how these events have affected certain aspects of asset sales under section 363 of the US Bankruptcy Code.

While the credit markets are more recently showing signs of repair, they remain far from returning to the halcyon days of near unlimited liquidity. In the meantime, lenders remain skeptical of asset values. In addition, many corporate borrowers today find themselves burdened by blanket liens that secure obligations to their lender groups, leaving few if any unencumbered assets to secure new credit. The usual suspects who once freely provided debtor-in-possession ("DIP") financing have retrenched or withdrawn entirely from this once vibrant market. Prospective borrower-debtors are seen today as riskier investments since there is often little consensus on asset values and less available collateral to guaranty repayment of any DIP Financing. As a result, many companies are finding that the path into and out of chapter 11 is more difficult and uncertain than debtors in previous downturns when DIP financing was more readily available.

The lack of liquidity in bankruptcy cases has left many debtors with no meaningful alternative other than to effect the prompt, orderly sale of their businesses and assets under section 363 of the U.S. Bankruptcy Code, often without any meaningful recovery for unsecured creditors. Classic restructurings that culminate in the confirmation of a plan of reorganization are more expensive and time consuming, and without available funding, many debtors today cannot afford those costs. Consider the words of Bankruptcy Judge James M. Peck of the United States Bankruptcy Court for the Southern District of New York during the confirmation hearing for the chapter 11 plan of Quebecor World (USA), Inc. ("Quebecor"), one of the few classic restructurings to have taken place of late:

> [Classic restructurings] are increasingly the exception. This is a case . . . that was not prepackaged and it included a DIP financing arrangement whose maturity was

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> coextensive with a period of exclusivity permitted under the bankruptcy code. A full 18 months. This was not a hurry up case. This was not a case in which outsiders sought arbitrarily to limit the time during Chapter 11. This was not a case in which assets were being sold quickly, left behind with cash to later distribute and litigate avoidance actions. This is a classic increasingly rare [sic] Chapter 11, a stand alone reorganization in which well represented constituents negotiated hard and long to achieve a reorganization which is really on the verge of a great success.[2]

2. TRENDS IN ASSETS SALES UNDER SECTION 363 OF THE US BANKRUPTCY CODE

Once considered the exception to classic restructurings, the sale of a debtor's business and assets as a going concern under section 363 is increasingly becoming the norm. Section 363 sales are fundamentally different than a reorganization in the classic sense described above by Judge Peck. For example, orderly section 363 sales are often effected within 60 days of the petition date. With the exception of true pre-packaged plans, pre-negotiated plans often take 90-120 days to confirm. A sale under section 363 also lacks the usual rights and protections afforded to creditors in the plan solicitation and confirmation process. When DIP financing is available today, increasingly it comes from private investment funds who are already invested in the debtor's pre-bankruptcy capital structure, rather than traditional bank lenders. Such funds often use the provision of DIP financing to influence the timeline and outcome of the chapter 11 case. Today, while court-supervised auctions continue to take place, bidders, particularly of the strategic variety, are a rare commodity. More frequently the party who agrees to serve as the stalking horse bidder wins the assets without having to top competing bids and often by credit bidding its secured claims against the debtor.

2.1 Loan-to-Own Approach

Today, the stalking-horse-bidder in a proposed sale of a debtor's assets under section 363 increasingly emerges from the ranks of the debtor's existing lenders and seeks to credit bid the secured claims it holds rather than making cash bids. Often these stalking-horse-bidders have invested in the debtor with the expectation that they will effect a bid for the debtor's assets in bankruptcy, the so-called "loan-to-own" approach ("<u>LTO</u>").

Variations on the LTO strategy were present in one form or another in the vast majority of recent section 363 sales we reviewed. Many of the would-be buyers either made loans to the debtor or purchased some of their debt with an eye toward eventually acquiring all of the debtor's assets. A classic example of this strategy is *In re WBE, LLC*,[3] where hedge fund D.B. Zwirn Special Opportunities Fund LP ("<u>D.B. Zwirn</u>") made pre- and post-petition loans to the debtor in an amount of approximately $36.5 million. D.B. Zwirn later credit bid $12.5 million of its secured debt as the stalking horse bidder and was determined to be the successful bidder when no competing bids were made.

The LTO investor is often the driving force behind the debtor's bankruptcy filing. The LTO investor will sometimes strategically position the debtor so that a chapter 11 filing is the debtor's best remaining option to maximize value for creditors through a section 363 sale of the debtor's assets. The ability to credit bid its debt claims in any such sale often gives the LTO investor a significant advantage over other bidders making cash offers. In *Big 10 Tire Stores Inc.*,[4] private

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[2] Transcript at 187, *In re Quebecor World (USA) Inc.*, No. 08-10152-jmp (Bankr. S.D.N.Y. June 30, 2009).

[3] *In re WBE, LLC*, No. 09-10649-mfw (Bankr. D. Del. filed Feb. 25, 2009) (debtor changed name to WBE, LLC while in bankruptcy).

[4] *In re BT Tires Group Holding, LLC*, No. 09-11173-css (Bankr. D. Del. filed April 2, 2009) (cases consolidated into that of parent holding company).

equity firm Sun Capital Partners Inc. both owned the equity of and had made pre- and postpetition loans to the debtor. Sun Capital served as the stalking-horse bidder for the debtor's assets, and proposed credit bidding its secured debt in the amount of $27.89 million and offering to assume certain liabilities. An auction was canceled after no other bids were submitted, and Sun Capital acquired the debtor's assets.

LTO investor driven sales are not without controversy. Bankruptcy Courts and commentators alike have suggested that the LTO investor may in some cases unduly influence the sale process. The LTO investor may constrain a company's ability to obtain new credit, leaving the company with no alternative to filing for bankruptcy protection. Some argue that an LTO investor who holds debt and equity interests in the debtor often has greater access and insight to the debtor's business than potential third party buyers. Given the compressed timetable for effecting most 363 sales (e.g., less than 60 days), other potential bidders may not believe they can overcome this perceived informational disadvantage and tailor their bids accordingly. Another complaint is that the LTO investor acquires the debtor's most valuable assets using debt claims often purchased at a substantial discount, while shedding many liabilities through the 363 process at the expense of unsecured creditors, who more frequently receive little or nothing as a result of the proposed sale. Given the relative advantages enjoyed by LTO investors, some have wondered whether bankruptcy courts are inappropriately providing their imprimatur to sweetheart, insider deals by approving these transactions.

Some 363 sales may appear improper where insiders or LTO investors are acting as the stalking horse bidder. When one considers the lack of options the debtor often faces as it becomes more financially distressed, however, one must ask whether there is anything inherently wrong with these sales.[5] Without the DIP financing that an LTO investor provides, many debtors would have no choice but to shut down their operations and convert to chapter 7. A successful 363 sale process instead allows the business (or at least parts of it) to continue to operate. Furthermore, the checks and balances of legal and financial advisors, including representation of unsecured creditors by the official committee of unsecured creditors, and the assurance of due process through court supervision of the sale, guard against abuse of the 363 sale process.

Indeed, the role of the Bankruptcy Court is, among other things, to determine if the buyer (whether an LTO investor or not) has acted in good faith and whether the proposed sale is the product of a full and fair marketing and sales effort based on the evidence presented at the sale hearing. Objecting creditors, who are often unsecured, complain that the sale process is almost always too short, and the stalking horse bidder has an unfair information and diligence advantage that cannot be overcome without more time. Objecting creditors also often characterize the proposed bid as woefully inadequate compared to the real value of the debtor's assets as a going concern. However, it is unusual for the objecting creditors to provide the additional funding that would be required to extend the sale process to their satisfaction. Where no other competing bidder has emerged and there are limited funds to finance the sale process, Bankruptcy Courts often have little choice but to conclude that the proposed sale is the highest and best offer for the debtor's assets (and a better result than a sale of assets under chapter 7).

The presence of an insider or LTO investor alone does not and should not invalidate a section 363 sale process, but parties can expect that the Bankruptcy Courts and creditors will apply greater scrutiny to the proposed sale and related process. Transparency in such cases often is the best disinfectant and should increase the likelihood of a smooth sale process. Moreover, considering that most often the debtor's alternative is chapter 7 liquidation, the proliferation of

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[5] For an interesting discussion of Loan-to-Own trends generally in an analysis of common creditor and equityholder objections to LTO transactions, *see* Jonathan M. Landers, *Reflections on Loan-to-Own Trends*, XXVI-8 AM. BANKR. INST. J. 1 (October 2007).

LTO deals and more frequent section 363 sales generally are not necessarily bad trends for creditors.

2.2 Credit Bidding

In the current climate, where financing is limited and the senior secured creditors are increasingly the fulcrum security, credit bidding by the senior secured lenders has become more frequent. This has brought forth interesting questions regarding what level of lender support is necessary in order to credit bid, or if the lenders are not the successful bidder at the auction, to release the liens on the assets. In *In re Chrysler, LLC*, 576 F.3d 108 (2d Cir. 2009) the minority lenders argued that 100% lender support was necessary to release the liens on collateral and waive the right to credit bid on the collateral. The United States Bankruptcy Court for the Southern District of New York found that, through the credit agreement and ancillary documents, had given their consent to allow the administrative agent to give its consent to dispose of the collateral, release all of the lenders' liens on the collateral, and waive the right to credit bid on the collateral, particularly at the direction of the requisite amount of lenders under the documents. Similarly, in *In re Metaldyne Corp.*, No. 09-13412-mg (Bankr. S.D.N.Y. filed May 27, 2009), a minority lender claimed that the administrative agent was not authorized to credit bid on behalf of such lender under the terms of the credit agreement. Relying heavily on the *Chrysler* decision, the United States Bankruptcy Court for the Southern District of New York held that under the credit agreement, the collateral agent had broad powers to dispose of collateral, including the right to credit bid the entirety of the loan with the support of the required lenders. In *In re Electroglas, Inc.*, No. 09-12416-psw (Bankr. D. Del. filed Sept. 23, 2009), certain minority lenders proposed to credit bid solely their portion of the debt. The United States Bankruptcy Court for the District of Delaware found that due to requirements in the bond indenture that the lenders were prohibited from taking action that would not treat all holders equally, a partial credit bid was not permissible. Additionally, the Bankruptcy Court found that under the specific language in the indenture, that required lenders could not force the trustee to take certain action, they could tell the trustee what to do procedurally, but it was up to the trustee whether or not to take a substantive action, such a credit bidding. Overall, the specific language in each credit document is likely to govern the outcome of cases when credit bidding is at issue. It will certainly be interesting to note whether future credit agreements are more explicit regarding minority rights related to credit bidding and release of liens in connection with section 363 sales.

Historically, a lender's right to credit bid has been viewed as an absolute. However, recently, a senior secured lender's right to credit bid in a sale process pursuant to a plan has been questioned. In *In re Philadelphia Newspaper, LLC*, No. 09-11204-sr (Bankr. E.D. Pa. filed Nov. 10, 2009), the debtors proposed to sell their assets to an insider stalking horse pursuant to a chapter 11 plan. The bid procedures precluded the secured lenders from credit bidding because, it was argued, a right to credit bid would chill bidding. The United States Bankruptcy Court for the Eastern District of Pennsylvania refused to approve the bidding procedures with the credit bidding preclusion. The debtor removed the preclusion and the procedures were approved. On appeal, the District Court found that the Bankruptcy Court erred in refusing to allow the preclusion.[6] The District Court looked to the plain meaning of section 1129(b)(2)(A) of the Bankruptcy Code, focusing on the use of the word "or" and the need for the debtor to meet only one of the three alternatives. The District Court differentiated between the "sale prong" set forth in section 1129(b)(2)(A)(ii), which provides for the sale of collateral free and clear of liens but subject to the right to credit bid, and the "indubitable equivalent prong" set forth in section 1129(b)(2)(A)(iii) that does not contain a reference to a section 363(k) right to credit bid. The District Court acknowledged that the debtor was left open to objections by the lenders at confirmation that sale process had not generated fair market value and thus they were not receiving the indubitable equivalent of their claim. The ruling was appealed to the Third Circuit and on March 22, 2010, the appellate court issued a decision agreeing with the District Court that

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6 *In re Philadelphia Newspapers*, 2009 U.S. Dist. LEXIS 104706 (E.D. Pa. 2009).

section 1129(b)(2)(A) is unambiguous and that a plain reading of its provisions permits the debtor to proceed under sub-section (iii) without allowing the lenders to credit bid. *In re Philadelphia Newspapers, LLC*, 09-4266 (3d Cir. Mar. 22, 2010).

2.3 No Apparent Trend To Allow Financing and Other Contingencies in Bids

One might expect that the seismic events that have roiled the credit markets would lead to bids in the section 363 context that increasingly contain financing "outs" or other contingencies once considered unacceptable. Except for the two cases mentioned immediately below, however, our research has not revealed a meaningful trend in this respect, so it seems debtors (and their creditors) continue to expect that the stalking horse bid and any competing bids will not contain conditions that would allow the buyer to walk-away after being designated the successful bidder.

In *In re Canal Corp.*,[7] for example, Irving Place Capital Management ("IPCM") and Oaktree Capital Management ("Oaktree"), joint stalking-horse bidders for the debtor's assets, won the auction for the debtor's assets despite certain financial contingencies in their bid. The debtor failed to secure the requisite financing, but IPCM and Oaktree agreed to waive their contingency rights and consummated the sale nonetheless. In this case, the stalking horse bidders were owners of the debtor's senior bank debt and agreed that if they walked away under certain circumstances, the debt would be contributed to the estate. Thus, the stalking horse bidders provided some level of protection for the debtor despite the financing out.

In *In re Lenox Sales, Inc.*,[8] the debtor filed a prepackaged plan that involved selling its assets to a group of the debtor's prepetition lenders. The lenders' bid, however, was contingent upon securing financing commitments that were not obtained before the bid deadline. After the debtor turned to other bidders, these lenders submitted a revised offer backed by a financing commitment, which the debtor then accepted. Again, despite the presence of a financing "out", the sale was ultimately consummated, suggesting that the "out" was related to execution risk rather than a desire not to consummate the deal.

We also reviewed a few cases where the facts involved bids that could possibly be described as contingent, but the contingencies seemed to relate more to the inherent execution risk rather than any provision of the bid that would give the buyer a financing "out". In other words, while a bid may appear firm on its face, if the bidder must arrange significant financing to effectuate the proposed transaction, the risk that the buyer cannot arrange financing could in effect be a financing contingency.

In *In re Hines Horticulture, Inc.*,[9] hedge fund Black Diamond Capital Management ("Black Diamond") served as the stalking horse bidder and was found to have made the highest and best offer for the debtor's assets when no competing bids were filed. While the bid contained no express financing contingency, and the sale ultimately closed, the parties had to agree to extend the closing deadline for several months because Black Diamond had difficulty arranging the necessary financing.

In *In re Eclipse Aviation Corporation*,[10] ETIRC Aviation S.a.r.l. ("ETIRC"), the debtor's majority shareholder and a significant creditor, attempted to purchase the debtors' assets and business as a going concern. ETIRC was the stalking horse bidder and was determined to be the successful bidder when no qualified competing bids were made. ETIRC had arranged financing through The Russian Federation Bank for Development and Foreign Economic Affairs. While there was no express contingency, the asset purchase agreement required that the parties close

[7] *In re Canal Corp.*, No. 08-36642-dot (Bankr. E.D. Va. filed Dec. 29, 2008).
[8] *In re Lenox Sales, Inc.*, No. 08-14679-alg (Bankr. S.D.N.Y. filed Nov. 23, 2008).
[9] *In re Hines Horticulture, Inc.*, No. 08-11922-kjc (Bankr. D. Del. filed Aug. 20, 2008)
[10] *In re Eclipse Aviation Corp.*, No. 08-13031-mfw (Bankr. D. Del. filed Nov. 25, 2008).

the sale within five days after the Bankruptcy Court's approval of the sale. The financing from Russia did not materialize before that time and the buyer failed to consummate the sale. Without an alternative bidder, and no funds to continue operations, the debtor converted its cases to chapter 7 cases. Again, the conditions in ETIRC's bid elevated the execution risk, but the bid nonetheless was a binding obligation of ETIRC.

In *In re TI Acquisition, LLC,*[11] the bidder declined to proceed with the purchase after the debtor failed to meet certain financial covenants. The bidder, Milliken & Co., set certain financial targets as a condition precedent to the bidder's obligation to close. When the debtor failed to meet those financial covenants, Milliken exercised its contingency and declined to proceed with the purchase.

While not a LTO case, *In re DG Liquidation Corp. (Diamond Glass Inc.)*[12] is notable. The case involved a pre-petition secured lender that was the DIP lender and stalking horse bidder for the debtor's assets. The buyer's proposed bid included its credit bidding a $34 million pre-petition secured claim against the debtor, plus funding a nominal cash component that would ensure a slight recovery for unsecured creditors. Most notably, the lender/bidder also offered to provide up to $25 million in acquisition financing to finance any potential competing bids. No bidder accepted the financing offer, but that feature, combined with the proposed distribution of proceeds for unsecured creditors, did much to dispel suggestions that the lender/bidder was trying unfairly to influence the sale process in its favor. The case concluded when a competing bidder topped the stalking horse bid, allowing the pre-petition lender to be paid in full on its claims against the debtor. We would not be surprised to see this strategy adopted in other chapter 11 cases where a bidder seeks to dispel arguments that it is unfairly influencing the sale process or where a lender's principal business is lending, not managing portfolio companies.

2.4 Is *Sub Rosa* Dead?

Some have questioned whether the rise of section 363 sales is killing arguments that sales are *sub rosa* plans. In *Braniff Airways*, the Fifth Circuit had stated that a debtor "should not be able to short circuit the requirements of Chapter 11 for confirmation of a reorganization plan by establishing the terms of the plan *sub rosa* in connection with the sale of assets."[13] Over the years, many creditors objecting to sale processes have used *sub rosa* arguments. The *Chrysler* court faced such arguments recently and looked to the findings of one of the seminal cases on 363 sales, *Lionel*, which had focused on the need to identify a "good business reason" for a 363 transaction.[14] In rejecting *sub rosa* arguments, both the Bankruptcy Court and the Second Circuit recognized that the proposed sale in no way upset the priority required by the Bankruptcy Code and that the equity stakes in New Chrysler were entirely attributable to new value (in the case of the unions, the value set forth in modifications to collective bargaining agreements governing future work) which were not assets of the debtor's estate. *In re Chrysler, LLC***,** 576 F.3d at 118. The *Chrysler* court found, based on this and other facts, that the sale was appropriate and did not constitute a *sub rosa* plan. Id. at 127. They did not, however, disregard the concept of *sub rosa* plans. In our view, arguments against *sub rosa* plans remain available to creditors to the extent the facts of a given case support them.

2.5 Must Secured Lenders "Pay to Play"?

In recent years, many chapter 11 cases have faced a scenario where recovery for unsecured creditors was unlikely and where there was even a potential for administrative insolvency.

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11 *In re TI Acquisition, LLC,* No. 08-42730-mgd (Bankr. N. Ga. filed July 27, 2008).

12 *In re DG Liquidation Corp.*, No. 08-10601-css (Bankr. D. Del. filed April 1, 2008).

13 *Pension Benefit Guar. Corp. v. Braniff Airways, Inc. (In re Braniff Airways, Inc.)*, 700 F.2d 935, 940 (5th Cir. 1983).

14 *Comm. of Equity Sec. Holders v. Lionel Corp. (In re Lionel Corp.)*, 722 F.3d 1063 (2d Cir. 1983).

Probably due to the relatively low values, many of these cases were run as quick sales under section 363 of the Bankruptcy Code. In some jurisdictions, these cases have raised the question of whether a secured lender, for whose benefit a case is arguably being run, must guarantee the payment of administrative claims, or "pay to play". Some parties have gone further and argued that secured lenders must make some concession to benefit unsecured creditors in order to keep the case in chapter 11.

Proponents of the "pay to play" requirement for unsecured creditors suggest that when the sale will generate proceeds that will be given solely to the secured lender, the lender should have to give something to get the benefit of chapter 11. After all, absent a chapter 11 case, the secured lender could just as easily foreclose and sell the assets itself outside of bankruptcy or the debtor could abandon the assets to the lenders. Those opposed to the requirement argue, among other things, that there is no such requirement embedded in the Bankruptcy Code and that if unsecured creditors are out of the money, it is irrelevant to them how the assets are administered. The argument against continues that secured creditors are "creditors" of a chapter 11 estate, their interests must be taken into account, and a process that maximizes the value of their collateral should be used, regardless of whether any other party receives any benefit.

There have been, and will continue to be, arguments on both sides of this issue. Without question, a fundamental purpose of chapter 11 is to maximize the value of the debtor's estate. There is nothing in the language of section 363 of the Bankruptcy Code that requires a sale to include a payment to unsecured creditors. In the absence of a clear answer, and given the desire on the part of lenders to have a sale occur quickly to avoid further use of cash collateral and/or diminution in value of the assets, creditors' committees have used such arguments, as well as other sale objections, to extract a "tip" from the lenders in order to gain their support for the sale in question. Given these types of settlements on the courthouse steps, clear authority may not be quick to develop on this point.

2.6 Are Valuations Being Deemphasized?

The growing trend of a preference for 363 sales over more costly and time consuming classic reorganization practice has given rise to the claim that the rise of 363 sales have played a significant factor in the decline of valuations. In a 2007 article published by Professors Lynn LoPucki and Joseph W. Doherty, the authors assert that valuations of debtors' for purposes of restructuring have been deemphasized.[15] LoPucki and Doherty go so far as to state that they are unaware of any modern cases in which a large public company proposed a 363 sale which was denied by the Court.

LoPucki and Doherty claim that there are several sale process characteristics that reduce the likelihood that unsecured creditors will object to a 363 sale, and that even if there were such an objection, that it would not succeed. First, according to LoPucki and Doherty, to know whether the sale price is inadequate, a party may be required to spend millions of dollars for an independent valuation and few unsecured creditors have a stake in the sale large enough to warrant such an expense. Second, the creditor's interest is unlikely to be a match for the debtor in a fight over whether to sell or reorganize. LoPucki and Doherty contend that debtors spend about four times as much in professional fees as do all of the Creditors Committees representing creditors and shareholders combined. "The greater expenditures, together with the information advantage that accrues from operational control, give debtors the upper hand."[16] Third, efforts to oppose a sale usually produce only conflict and delay to the unsecured creditor's further disadvantage, and according to LoPucki and Doherty, the Bankruptcy Courts are unlikely to rule in the creditor's favor, even when their objections are well-taken.

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15 Lynn M. LoPucki, Joseph W. Doherty "Bankruptcy Fire Sales", 106 Michigan Law Review 1 (Oct. 2007).

16 *Id.* at page 22.

Not all commentators agree with LoPucki and Doherty theories on sales versus reorganization. One proposition is that a more plausible explanation for the lower prices obtained in 363 sales versus reorganizations is that the companies that are forced to sell their assets in 363 sales are different from companies that are able to reorganize.[17] In other words reorganizable companies often have the support of their secured creditors while the companies that must conduct Section 363 sales typically do not have that support. These companies may lack creditor support because of bad management and/or business prospects. Out of money, secured creditors and unsecured creditors may argue for reorganization but unless they are willing to provide funding for a reorganization, the only alternative may be a going concern sale in chapter 11 or piecemeal sale in a chapter 7. Secured creditors can either watch their collateral deteriorate in value while waiting for an incompetent management to propose an unverifiable plan or they can force a section 363 sale. In these situations, values appear to be deemphasized to enable a debtor to conduct a going concern sale as opposed to shutting down the debtor and liquidating its assets piecemeal.

A number of recent cases exemplify the Court's willingness to rely on the free market while deemphasizing valuations of a debtor's assets. In *Onsite Sourcing, Inc*.,[18] Integron Managed Solutions ("Integron"), a secured creditor, purchased bank notes prior to the debtor's bankruptcy filing aimed at strategically expanding its existing business. The Court approved the sale while finding that the total amount Integron paid the debtor for its assets represented the fair value of the assets on the day they were purchased. According to the Court, fair market value of an asset is the value at which a willing buyer is willing to pay, and a willing seller is willing to sell. The Court approved the sale despite that Integron was a pre-determined purchaser.

Other cases decided this year, including *On Site Sourcing, Inc*. and *Gulf Coast Oil Corporation*[19], have followed a nine-factor test when determining whether to grant a 363 sale. These factors are: (1) is there evidence of a need for speed?; (2) what is the business justification?; (3) is the case sufficiently mature to assure due process?; (4) is the proposed asset purchase agreement (APA) sufficiently straightforward to facilitate competitive bids, or is the purchaser the only potential interested party?; (5) have the assets been aggressively marketed in an active market?; (6) are the fiduciaries that control the debtor truly disinterested?; (7) does the proposed sale include all of the debtor's assets, or does it include the "crown jewel"?; (8) what extraordinary protection does the purchaser want?; and (9) how burdensome would it be to propose a sale as part of the confirmation of a chapter 11 Plan? Findings such as immediate control by a purchaser is required to avoid loss of value of the assets will give rise to a valid 363 sale.

In presiding over the Chrysler bankruptcy proceedings,[20] Chief Bankruptcy Judge Arthur Gonzalez reiterated that in the past twenty-five years, "asset sales under Section 363 have become the preferred method of monetizing the assets of a debtors company." The shift to 363 sales is driven by efficiency. The speed of the 363 sale can help maximize asset value of the debtor, free and clear of all liens, claims, interests and encumbrances, while the buyer can select the liabilities to assume. One example of the efficiency of 363 sales is Lehman Brothers[21] in which the debtor sold substantially all of its assets within five days of filing for Bankruptcy to

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[17] Joseph S. Athanas, "Section 363 Bankruptcy Sales Attacked by Judges and Commentators Just as Economic Conditions Make Them More Important than Ever," Bankruptcy and Restructuring Chapter 11 Strategies 2009, 2009 W.L. 531546 (ASPATORE) (2010)

[18] *In re Onsite Sourcing, Inc.*, No 09-10816-rgm (Bankr. E.D. Va. filed June 22, 2009).

[19] *In re Gulf Coast Oil Corporation*, Nos. 08-50213, 08-50215 (Bankr. S. D. Tex. filed February 11, 2009).

[20] *In re Chrysler, LLC*, 405 B.R. 84 (Bankr. S.D.N.Y. 2009), vacating as moot, 2009 WL 2844364 (2009) (per curium) and cert. dismissed 130 S. Ct. 41 (2009) (Mem.).

[21] *In re Lehman Brothers Holdings, Inc.*, No. 08-CV-8869 (dlc) (Bankr. S.D.N.Y. 2009).

Barclay's for $1.7 billion. The Court once again relied on the free market and sale price to determine the fair market value for Lehman Brothers assets.[22]

2.7 Other Observations

Our research has also illustrated the uncertainty in the bankruptcy context generated by government intervention. Government involvement can in some cases result in a speedy prepackaged 363 sale, as in *In re General Motors Corporation*,[23] but it can also have seemingly no effect at all, as happened in *In re Delphi Corp.*[24] where the sale and plan backed by the government had little effect on the process in that Delphi was sold to another bidder. Until the global recession subsides and the credit markets take greater steps towards "normal" activity levels, the specter of government intervention in chapter 11 cases will continue at least in cases where the debtor is said to be too-big-to-fail or otherwise of strategic importance to the overall economy.

3. CONCLUSIONS

As a result of the difficult economic environment over the last couple of years, bankruptcy filings have been on the rise. Faced with difficulty securing DIP financing and few other options, many debtors have chosen to pursue asset sales under section 363 of the Bankruptcy Code. Increasingly, lenders of various types, including those that own equity in the debtors, have used their creditor positions to acquire debtors' assets through such sales. While some of the resulting transactions have been cause for skepticism, we are not convinced that the increase in such sales is a worrisome trend. Additionally, a few instances of financing and other contingencies in 363 sale bids have arisen, but we believe these instances are isolated and are not indicative of a trend away from closing certainty. Further, with the rise of 363 sale, valuations are being deemphasized and instead, courts are relying on the auction process to determine fair market value. Finally, government intervention in the bankruptcy space has increased uncertainty as to what role the government will play in future bankruptcies.

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22 We note that Lehman Brothers Holdings, Inc. has since filed a lawsuit against Barclays Capital, Inc. ("Barclays") alleging, among other things, that Barclays took control of excess assets and failed to assume certain liabilities by colluding with certain Lehman executives. This litigation however is in its infancy, so it is too early to comment on the outcome.

23 *In re General Motors Corp.*, No. 09-50026 (Bankr. S.D.N.Y. filed April 30, 2009).

24 *In re Delphi Corp.*, No. 05-44481-rdd (Bankr. S.D.N.Y. filed Oct. 8, 2005).